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China - Peoples Republic of Grain and Feed Update

Reform Continues in the Corn Sector

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Report Highlights:

Harvest is underway for spring/summer crops. The 2017/18 corn production forecast is raised on better yield, improved seed quality, and favorable weather during the growing season. The PSD tables for feed grains (corn and sorghum) are updated for 2016/17 based on trade to date and for 2017/18 on expectations of greater consumption. There are minor updates for food grains (wheat and rice). Over the summer, there have been several announcements that could impact the grain sector, particularly for corn. The most recent announcement, the goal to adopt E10 usage in gasoline by 2020, if realized, could sharply boost corn consumption and reduce stocks. When combined with the ongoing reform, China could find itself tight in corn just in a few years.

Post:
Beijing

Policy

VAT Simplified; Appreciation of RMB boosts Imports

Following the May 2017 announcement by the Ministry of Finance, the 4 tier value-added tax (VAT) regime has been consolidated into 3 tiers - 17, 11, and 6 percent rates, eliminating the 13 percent rate. Effective July 1, the VAT for agricultural products, including grains, has been reduced from 13 to 11 percent.

The Chinese currency, RMB, has steadily appreciated against the U.S. dollar this year. The exchange rate in January was 6.94 RMB to US\$1; in July, it was around 6.72 RMB; and in the early September, the rate was 6.49 RMB. Strong imports have been attributed to the reduced VAT combined with the appreciation of RMB.

Restrictions for Foreign Investment in the Agricultural Processing Sector Removed

In June 2017, the National Development and Reform Committee and the Ministry of Commerce released the 2017 Foreign Investment Industrial Guidance Catalogue. It removed restrictions on foreign investment in the processing of oilseeds, sugar, rice, flour, and deep processing of corn.

Development of Animal Agriculture in Grain Producing Areas

In early August, the Ministry of Agriculture (MOA) published its opinion “Accelerating the Development of Modern Animal Husbandry in the Main Grain Producing Areas of Northeastern China.” It stresses to accelerate the development of modern animal husbandry in Northeast to consume corn stocks, and suggests firms seize this right time as feed cost has eased after the corn policy reform. The opinion encourages the Northeast region to develop livestock breeding and feed industries.

Subsidies for Silage and Less Grain Corn Planting Announced

In August, the Heilongjiang Farm & Land Reclamation Administration published a notice announcing up to 60 RMB per ton (equivalent to 240 RMB per mu) subsidies for silage corn, up to 120 RMB per ton for half-dried silage feed oat, and up to 240 RMB per ton for half-dried alfalfa silage.

In a September press conference, MOA stated that China has reduced more than 30 million Mu of corn planting area in 2016, of which 10 million Mu was shifted to soybeans. For 2018, MOA expects more than 20 million Mu (1.3 million hectares) in reduction of sown area for corn.

In its Grain-to-Feed Implementation Plan, MOA encourages corn growers in the “reaphook”- shaped regions and Huang & Huai & Hai Rivers regions, which include 17 provinces and the Heilongjiang Farm & Land Reclamation Administration, to shift from planting grain corn to crops such as silage corn, alfalfa, oats, sweet sorghum, and legumes. (Note: China has 23 provinces, 4 municipalities, 5 autonomous regions, and 2 special regions)

Calls to Lower Minimum Support Price (MSP) for Wheat and Rice

There have been steady calls from government researchers and academics to lower or suspend the MSP for wheat and rice this year. At the China Grain Forum, researchers from the State Council urged the

government to lower the MSP for wheat (from 2,360 to 2,300 RMB per ton) starting from 2018; to lower the MSP for japonica rice (from 3,000 to 2,800 RMB per ton) and the MSP for mid-to-late season indica rice (from 2,720 to 2,600 RMB per ton); and to suspend the MSP for early indica rice, which accounts for 70 percent of rice stocks. Also, researchers warned, given the ongoing corn sector reform, holding the MSP constant could cause corn areas in Northwest shift to wheat and corn areas in Northeast shift to rice, adding pressure to already large stocks. Post expects corn areas in Northeast will more likely shift to soybeans.

Supply-side Reform on Agriculture Announced

The State Council issued a circular in the early September calling for faster development of grain industry and a supply-side structural reform to enhance agricultural efficiency and to boost farm incomes. The circular sets a target of building a modern grain industrial system by 2020, and projects to have at least 50 grain enterprises with main business revenue surpassing 10 billion yuan (\$1.5 billion). It aims to reform state-owned enterprises (SOEs) to promote competitiveness among them and to ensure food security. It also encourages grain companies to take advantage of location and resources when exploring business ideas; to integrate supply and distribution channels throughout production, purchases, storage, and sales; to develop e-commerce (“Internet Plus Grain”); and to strengthen brands, patents, and trademarks to eliminate counterfeit products. The State Council’s news release is found in the link: http://english.gov.cn/policies/latest_releases/2017/09/08/content_281475844814324.htm

The Goal of E10 Use by 2020:

On September 13, 2017, the state media reported on “The implementation plan regarding the Expansion of Ethanol Production and Promotion for transportation fuel (关于扩大生物燃料乙醇生产和推广使用车用乙醇汽油的实施方案).” The plan was jointly announced by the National Development and Reform Commission (NDRC), the National Energy Administration, the Ministry of Finance and 12 other Ministries. According to the plan, China will achieve nationwide use of E10 (10 percent fuel ethanol and 90 percent gasoline) in transportation fuel by 2020. By 2025, China will shift to produce cellulosic ethanol by using grasses, forest waste, and crop residues. The state media noted that adopting E10 is imperative to reduce excessive corn stocks and reduce air pollution. The NDRC stated that China’s annual fuel ethanol use will reach 10 million metric tons by 2020 in its “Renewable energy long term development plan (可再生能源中长期发展规划).”

Please note that China does not publish official data on transportation fuel ethanol production. There is a variation in private estimates, ranging around 1-3 million tons, less than one-third of the 2020 target. According to the National Bureau of Statistics, China’s gasoline consumption in 2016 totaled 120 million tons. The E10 target implies that China would need to produce 12 million tons of transportation fuel ethanol just in 3 years. This will require 36 million tons of corn. Industry sources noted that even if the existing capacity is fully used, the additional operation would only boost the national production by about 30-35 percent, well short of the target. Ethanol production using corn will yield sizable amount of distillers’ dried grains (DDGS), which could be used for animal feed, competing against imported sorghum and barley.

The announcement stated that the primary goal for the adoption of E10 is to reduce excessive corn stocks. The potential increase in corn use for transportation fuel ethanol production could help achieve

this primary goal. Meanwhile, multiple measures have been in place to reduce corn supply and to increase consumption. When combined, the ongoing reform and the E10 target could squeeze the availability of corn in just a few years.

Corn

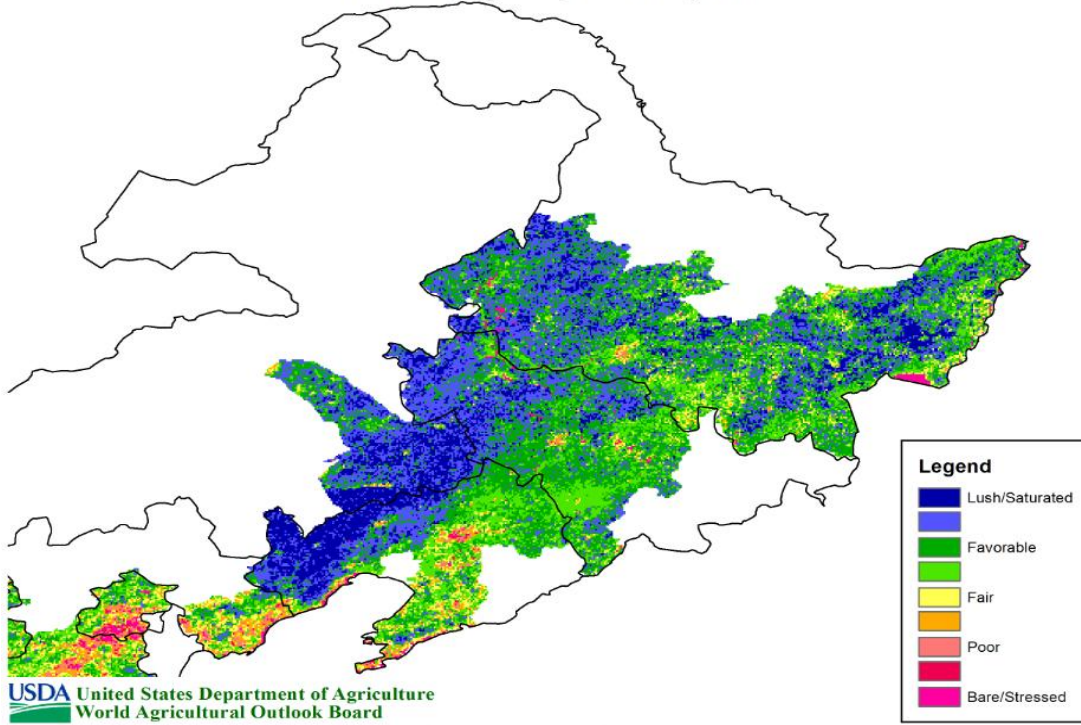
Corn Market Begin Year China	2015/2016		2016/2017		2017/2018	
	Oct 2015		Oct 2016		Oct 2017	
	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post
Area Harvested	38119	38119	36760	36760	35000	35000
Beginning Stocks	100472	100472	110774	110774	101278	101248
Production	224632	224632	219554	219554	215000	215000
MY Imports	3174	3174	3000	3000	3000	3000
TY Imports	3174	3174	3000	3000	3000	3000
TY Imp. from U.S.	321	321	0	0	0	0
Total Supply	328278	328278	333328	333328	319278	319248
MY Exports	4	4	50	80	20	50
TY Exports	4	4	50	80	20	50
Feed and Residual	153500	153500	162000	162000	166000	166000
FSI Consumption	64000	64000	70000	70000	72000	74000
Total Consumption	217500	217500	232000	232000	238000	238000
Ending Stocks	110774	110774	101278	101248	81258	79198
Total Distribution	328278	328278	333328	333328	319278	319248
Yield	5.8929	5.8929	5.9726	5.9726	6.1429	6.1429
(1000 HA) ,(1000 MT) ,(MT/HA)						

MY 2017/18

Post raises the 2017/18 **production** estimate on better than expected yield. Despite a dry start to the northeastern growing season, timely rainfall in mid-June improved soil moisture and crop conditions in Jilin and Liaoning. The Vegetative Health Index (VHI) below illustrates favorable to lush conditions across major corn areas of northeastern region, which accounts for nearly 40 percent of the nation's corn production. In addition, the percent of the crop that is estimated at good to excellent (based on the VHI) is above 50 percent (75 percent or more in Heilongjiang, Jilin, and Inner Mongolia) and better than last

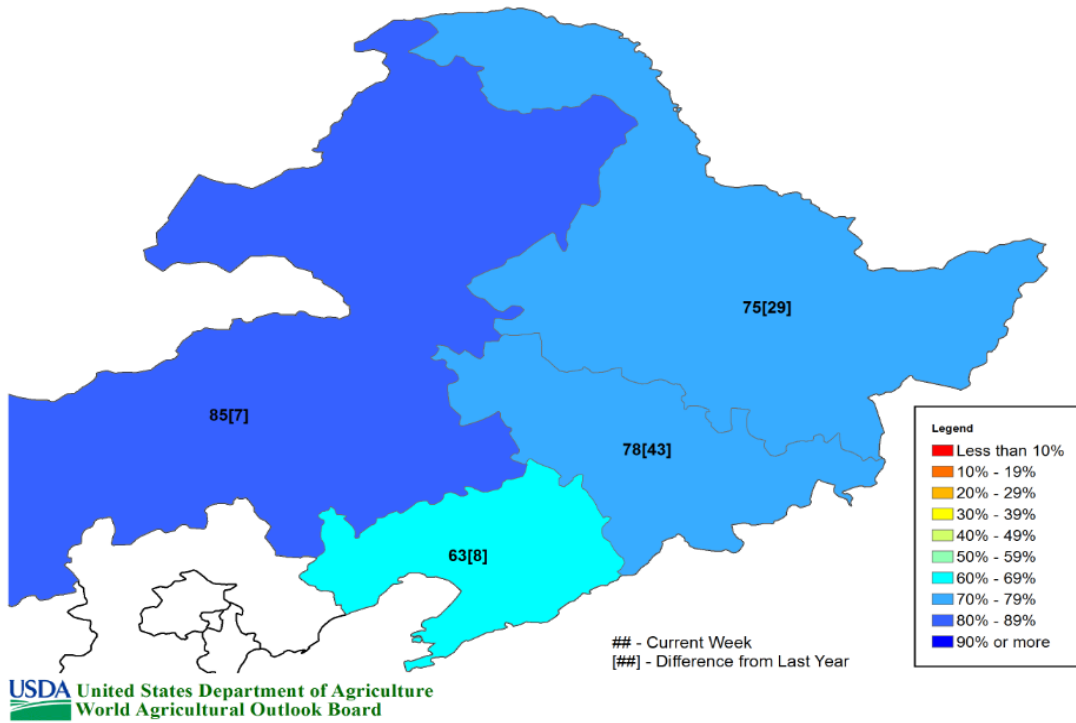
year throughout the northeast, with the largest year-to-year improvements in the two largest producing provinces of Heilongjiang and Jilin.

Vegetative Health Index: Northeastern China Major Corn Area
Week Ending: September 9, 2017



Northeast China Corn Condition

Percent Good to Excellent
 September 9, 2017



On **trade**, imports are doubled from the previous post estimate, and are the same level as the August USDA estimate. Strong demand for feed and deep-processing in the Northeast (Heilongjiang, Jilin, Liaoning, and Inner Mongolia) provinces will likely limit domestic corn moving to the Northern (Shandong, Henan, and Hebei) and Southern (Guangdong) provinces. These regions will likely turn to imports. Estimates for exports are unchanged from the previous post estimate.

Consumption, particularly Food, Seed, Industrial (FSI) consumption, is raised to reflect planned expansions in the deep processing industry. Aside from announcements by the government, industry sources mentioned various expansions in deep processing capacity in the next few years, particularly in the Northeast provinces. About 10 projects are currently underway, and are in various stages of development – from public announcements to under construction. About half of these projects are expected to complete their construction by the end of 2018. According to sources, most of the projects are located in the Heilongjiang province, while others are in Liaoning, Jilin, and Inner Mongolia. When all these projects are in operation, they could use about 10 -15 million tons of additional corn a year.

MY 2016/17

Production and consumption remain unchanged.

Imports are raised to 3 million tons reflecting large shipment in July. China imported 914,000 tons in July from Ukraine and from the United States. Large imports are attributed to competitive prices relative to domestic corn. Industry sources noted that strong imports could also be attributed to the processing subsidies in the Northeast provinces (Heilongjiang, Jilin, Liaoning, and Inner Mongolia). Earlier 2017, the Northeast provinces offered 100-300 RMB per ton to processors who purchased corn before April 30 and processed by June 30. The subsidy stimulated processing operations in the Northeast region, but tightened supplies in North (Shandong, Henan, and Hebei) and in South (Guangdong province) regions.

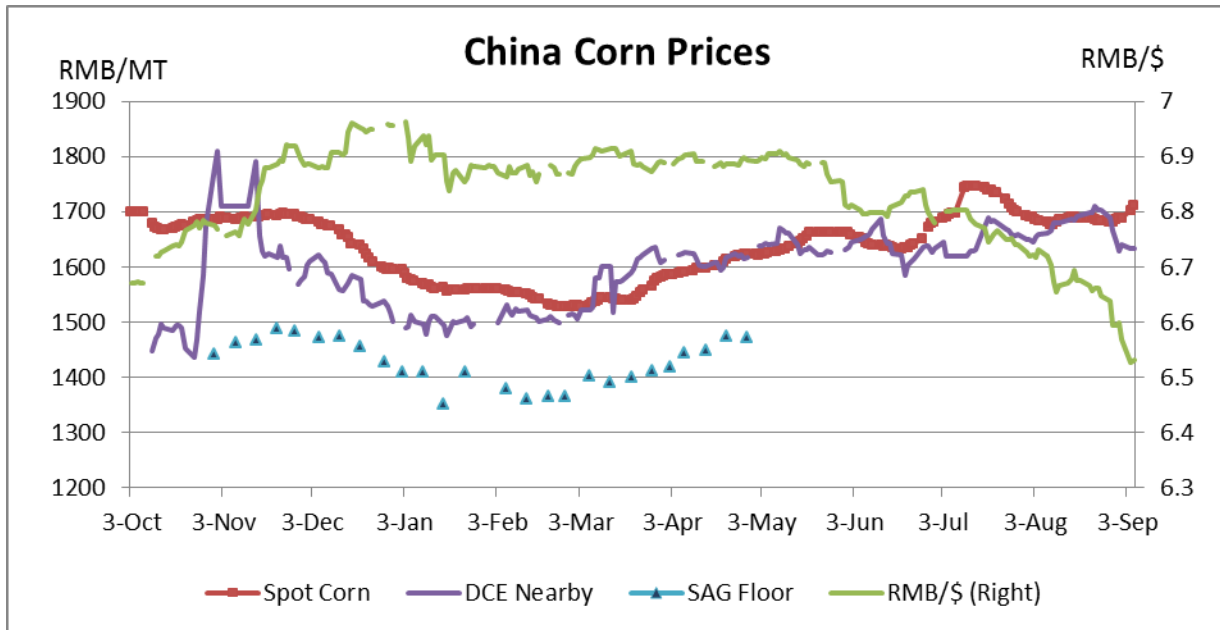
Exports are raised 30,000 tons to 80,000 on larger shipments to North Korea. While China's grain corn exports remain insignificant, exports of corn based industrial products have increased substantially just in a few years, indicating the revival of industrial consumption. Industry sources stated that there is a huge potential for China to advance deep-processing of corn, noting that China makes only a few hundred industrial products, compared to developed countries that make several thousand products using corn.



Prices

Domestic corn prices declined slightly in August as processing plants slowed down or suspended production for maintenance/upgrades to comply with stricter environmental standards. Consequently, prices for corn starch went up 200-300 RMB per ton. Prices for starch-based sweeteners also moved up combined with seasonal beverage demand. Likewise, ethanol and DDGS production slowed down, leading to relatively tighter supplies and higher prices. The environmental regulation scrutiny ended in August.

In September, corn prices have moved up with returning demand for processing operations. As harvest has yet to pick up pace in the Northeast, some farmers have been reluctant to sell their crop expecting higher prices. Overall, domestic corn prices are expected to remain elevated on strong demand for processing.



Sources: Industry Sources; Dalian Commodity Exchange; State Administration of Grain (SAG); Pacific Exchange Rate Service

Note: Since the removal of the minimum support price in the fall of 2015 and the subsequent market reform in the spring of 2016, there has been no formal price floor or temporary reserves for corn. Nevertheless, informal government intervention remains significant. The State Administration of Grain sets the floor price, and issues orders to state-owned enterprises, processors, and banks to buy sufficient volume of corn directly from farmers in the Northeast region. This is to ensure farmers sell their corn. It is believed that most of this corn goes into commercial channels.

Delivered Corn Spot Prices: September 5, 2017			
Province	Minimum	Maximum	Average
	RMB per ton	RMB per ton	USD per ton
<i>Northeast China</i>	1700	1750	\$264
<i>North China Plain</i>			
Shandong	1740	1780	\$269
Hebei	1800	1820	\$277
Henan	1800	1840	\$279
<i>South China</i>			
Guangdong	1750	1770	\$269

Source: CNGOIC and Post Calculations

Duty Paid Landed Price of U.S. Corn (on September 6)

Shipping Schedule	Estimated Duty Paid Landed Price	Domestic Corn Spot/Futures Price	Price Margin
August	¥ 1,422	¥ 1,687 (spot price on August 31)	¥ 265
September	¥ 1,509	¥ 1,713 (spot price on September 6)	¥ 204
September	¥ 1,509	¥ 1,654 (futures)	¥ 145
October	¥ 1,535		
November	¥ 1,541	¥ 1,674 (futures)	¥ 133
December	¥ 1,561		
January	¥ 1,579	¥ 1,720 (futures)	¥ 141

Source: Cofeed and Dalian Commodity Exchange

Sorghum

Sorghum Market Begin Year	2015/2016		2016/2017		2017/2018	
	Oct 2015		Oct 2016		Oct 2017	
	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post
China						
Area Harvested	574	574	760	760	780	780
Beginning Stocks	706	706	717	717	702	882
Production	2750	2750	3800	3800	3850	3850
MY Imports	8284	8284	4700	5200	4450	5000
TY Imports	8284	8284	4700	5200	4450	5000
TY Imp. from U.S.	6218	6218	0	0	0	0
Total Supply	11740	11740	9217	9717	9002	9732
MY Exports	23	23	15	35	10	30
TY Exports	23	23	15	35	10	30
Feed and Residual	8800	8800	6000	6300	5950	6300
FSI Consumption	2200	2200	2500	2500	2500	2600
Total Consumption	11000	11000	8500	8800	8450	8900
Ending Stocks	717	717	702	882	542	802
Total Distribution	11740	11740	9217	9717	9002	9732
Yield	4.7909	4.7909	5	5	4.9359	4.9359

(1000 HA) ,(1000 MT) ,(MT/HA)									

Production

MY2017/18 sorghum area and production are unchanged from the August USDA estimate. Despite dryness in certain areas, the Northeast region has reportedly received adequate rainfall.

Trade

MY2016/17 imports are estimated at 5.2 million tons, up 500,000 tons from the USDA August estimate based on trade to date. From October 2016 to July 2017, China imported 4.5 million tons, mainly from the United States and Australia. Competitive prices are also expected to support imports for the remainder of 2016/17. In addition, with the drop in imports of distillers’ dried grains (DDGS), feed users have turned to imported sorghum and barley in an effort to meet their needs. Sorghum imports for 2017/18 are forecast at 5.0 million tons on expectations of continued steady demand in the absence of DDGS. Exports for 2016/17 are revised up reflecting trade to date, and boosted slightly for 2017/18 on expectations that Taiwan remains the key destination.

Consumption

With greater imports, 2016/17 consumption is raised higher from the USDA August estimate. Industry sources commented that feed demand in the swine sector is in recovery. The baiju industry is also recovering from the government anti-corruption campaign, which started in 2012. According to a recent Xinhua news article, China’s leading brand Maotai will triple its baiju distribution from 20 million tons to 62 million tons for the upcoming Mid-Autumn Festival and the week-long national holidays in October to satisfy consumer demand and to prevent speculative buying. For 2017/18, consumption is expected to increase slightly from a year ago with greater use for feed and FSI, in particular, alcohol production.

Price

Industry sources noted that domestic sorghum prices are at three-year high. Prices for imported sorghum in South China ports have averaged CIF RMB 1,837 per ton, about RMB 400 (\$60) lower than domestic sorghum.

Wheat

Wheat Market Begin Year China	2015/2016		2016/2017		2017/2018	
	Jul 2015		Jul 2016		Jul 2017	
	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post
Area Harvested	24140	24140	24190	24190	24200	24200
Beginning Stocks	76105	76105	97042	97042	111392	111054
Production	130190	130190	128850	128850	130000	130000
MY Imports	3476	3476	4800	4410	3000	3000
TY Imports	3476	3476	4800	4410	3000	3000
TY Imp. from U.S.	613	613	1768	1768	0	0
Total Supply	209771	209771	230692	230302	244392	244054
MY Exports	729	729	800	748	800	800
TY Exports	729	729	800	748	800	800
Feed and Residual	10500	10500	16500	16500	13000	13000
FSI Consumption	101500	101500	102000	102000	103000	103000
Total Consumption	112000	112000	118500	118500	116000	116000
Ending Stocks	97042	97042	111392	111054	127592	127254
Total Distribution	209771	209771	230692	230302	244392	244054
Yield	5.3931	5.3931	5.3266	5.3266	5.3719	5.3719

(1000 HA) ,(1000 MT) ,(MT/HA)

MY 2017/18

There are no changes in area, **production, trade, or consumption**. Lower carryin stocks are due to trade changes in 2016/17 based on the China Customs.

In August, China has established a site in the Henan province to produce hybrid wheat seed in commercial scale. Wheat has been the only food crop without a large-scale hybrid seed production site. As a key research project under the 13th Five Year Plan, the site will support 5 million mu (330,000 hectares) of wheat area nationwide by the end of 2020.

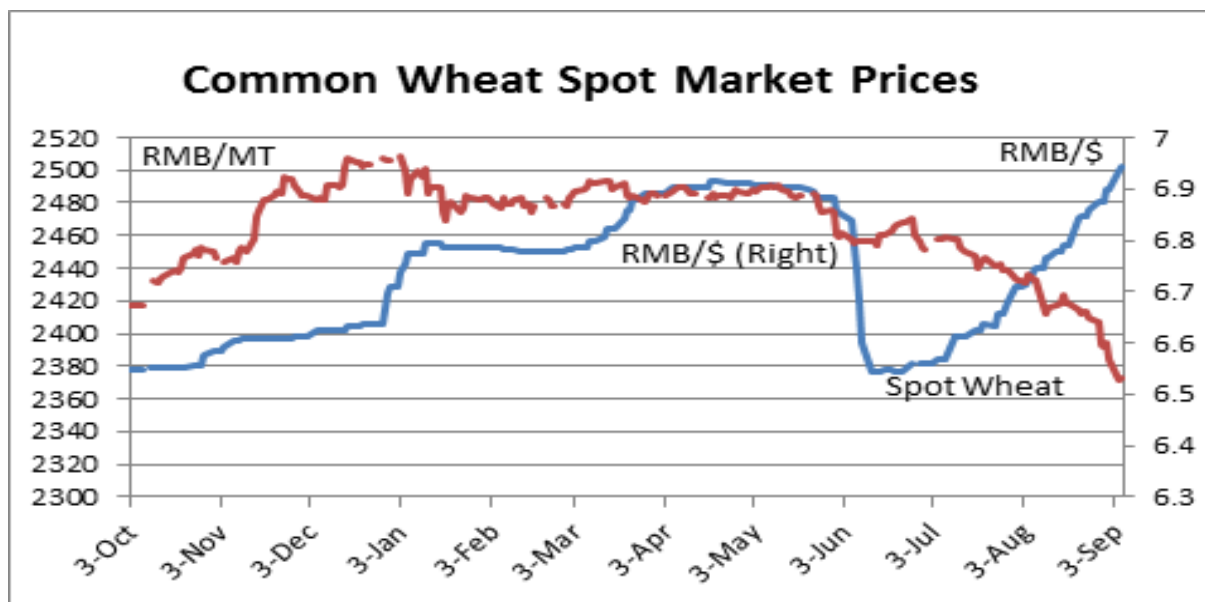
Wheat **prices** remained relatively strong in August. Reportedly, farmers are reluctant to sell their crop on expectations that prices would move higher when flour mills boost production in preparation for the

upcoming holidays. Wheat flour prices have increased RMB 20-120 per ton to RMB 2,920-3,480 (\$442-\$527). Both wheat and flour prices are expected to remain strong in the next few months.

As of September 5, the State Administration of Grain purchased 67.2 million tons of total wheat this year, about 1.0 million tons less than the same period a year ago. In July, all the six major wheat producing provinces - Hebei, Jiangsu, Anhui, Shandong, Henan, and Hubei- have started procurement at minimum price of RMB 2,360 (\$350) per ton. The procurement period ends on September 30. In October, the National Development and Reform Committee (NDRC) will announce the minimum price for the next year.

Wholesale Wheat Spot Prices in Major Markets				
Province	Common Wheat		Strong Wheat	
	--RMB per ton--	--\$ per ton--	--RMB per ton--	--\$ per ton--
Hebei	2,490	\$377	2,640	\$400
Shandong	2,480	\$376	2,660	\$403
Henan	2,480	\$376	2,650	\$402
Jiangsu	2,420	\$367	2,620	\$397
Anhui	2,450	\$371		

Sources: Industry sources



MY 2016/17

There are no changes in **production** and **consumption**. **Imports**, mainly from Australia and the United States, have been very strong in the latter half of 2016/17. One of the key reasons was quality problems in the 2016 wheat crop, resulting in greater demand for high-quality and high-protein wheat (such as U.S. Hard Red Spring) for blending. Demand has also been robust from the thriving baking industry in South China. In addition, soft wheat is also being imported for use in traditional Cantonese dim sum, such as sweet steamed buns. With domestic wheat production being located primarily in Eastern and

Northern China, two-thirds of all wheat imports in recent years were through ports in South China. Stocks are adjusted accordingly.

Rice

Rice, Milled Market Begin Year	2015/2016		2016/2017		2017/2018	
	Jul 2015		Jul 2016		Jul 2017	
China	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post
Area Harvested	30210	30210	30160	30160	30200	30200
Beginning Stocks	57436	57436	63735	63735	69430	69430
Milled Production	145770	145770	144850	144850	145000	145000
Rough Production	208243	208243	206929	206929	207143	207143
Milling Rate (.9999)	7000	7000	7000	7000	7000	7000
MY Imports	4800	4800	5150	5150	5000	5000
TY Imports	4600	4600	5100	5100	5000	5000
TY Imp. from U.S.	0	0	0	0	0	0
Total Supply	208006	208006	213735	213735	219430	219430
MY Exports	271	271	805	805	900	900
TY Exports	368	368	900	900	1000	1000
Consumption and Residual	144000	144000	143500	143500	143000	143000
Ending Stocks	63735	63735	69430	69430	75530	75530
Total Distribution	208006	208006	213735	213735	219430	219430
Yield (Rough)	6.8932	6.8932	6.861	6.861	6.859	6.859

(1000 HA) ,(1000 MT) ,(MT/HA)

There are no changes in the PSD table from the USDA August estimate.

Trade

In 2016/17 China's milled rice exports nearly tripled from the previous year driven by large shipments to many African countries on commercial terms as well as for donations.

In July 2017, China and the United States signed the agreement that allows U.S. rice exports to China. However, there remain a few outstanding steps that have to be completed before trade to start - China's audit of U.S. export facilities by the General Administration of Quality Supervision, Inspection and Quarantine (AQSIQ) and the registration of U.S. exporting companies with the AQSIQ. AQSIQ visits to audit U.S. export facilities have yet to occur as of this writing.

The State Council's think tank, the China Center for International Economic Exchange, has recommended investments in Thailand, Vietnam, Cambodia, and Pakistan to improve rice production and trade under the One Belt One Road initiative, China's global trading strategy. Already, China has invested in a hybrid rice research center in Pakistan to enhance Pakistani rice production and import into China via the China-Pakistan Economic Corridor.

The State Administration of Grain announced that more high-quality breeds of early indica rice have been planted resulting in improved quality, higher market price, and lower procurement by the government compared to a year ago. Reflecting the situation, procurements for early indica rice have started only in Jiangxi and Hunan provinces (out of 5 provinces) with the following specifications. The procurement period is August through the end of September.

State Administration of Grain: Standards for Rice

	Third-Class Early Indica Rice	Third-Class Mid-to-Late Indica Rice	Third-Class Japonica Rice
Minimum Price	\$382/ton (RMB 2600)	\$406/ton (RMB 2720)	\$441/ton (RMB 3000)
Moisture	less than 13.5%	less than 13.5%	less than 14.5%
Foreign Matter	less than 1%	less than 1%	less than 1%
Milling Rate	greater than/equal to 75% but lower than 77%	greater than/equal to 75% but lower than 77%	greater than/equal to 77% but lower than 79%
Unbroken Rice, milled	greater than/equal to 44% but lower than 47%	greater than/equal to 44% but lower than 47%	greater than/equal to 55% but lower than 58%

Average Indica Rice Spot Wholesale Prices in Early September, 2017

Province/Region	RMB per ton	USD per ton
Northeast	¥ 4,890	\$741
Hubei	¥ 4,393	\$666
Fujian	¥ 4,000	\$606
Jiangxi	¥ 4,025	\$610
Zhejiang	¥ 4,650	\$705

Source: Cofeed

Average Japonica Rice Spot Wholesale Prices in Early September, 2017

Province/City/Region	RMB per ton	USD per ton
Northeast	¥ 4,345	\$688
Fuzhou	¥ 4,635	\$702
Guangzhou	¥ 4,180	\$633
Hunan	¥ 4,380	\$664
Jiangsu	¥ 4,330	\$656

Shandong	¥ 4,300	\$652
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Source: Cofeed

