

Market is Strong for California Processing Tomatoes

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Normally a bumper crop in agriculture leads to lower prices, but not always. In 2007 California's processing tomato growers harvested a near-record crop and yet prices are rising. The international demand for California's tomato paste is strong and 2008 could be another good year for the processing tomato industry if Mother Nature cooperates.

The prospects for California's processing tomato industry have been turning positive over the last several years, and the economic situation has improved even more in 2007–2008 for growers and processors in the Golden State. Back in 2000, some industry observers predicted demise for the processing tomato market in California due to fears of excess processing capacity, oversupply, low farm gate prices, declining per capita domestic demand, and lack of international competitiveness. Those who were then writing an obituary for the California industry could not have been more wrong. Prices are now strong, acreage and processing capacity are expanding, and exports are on the rise. This is all coming together in a year when the size of the California crop is near record levels. Figure 1 shows that the 2007 U.S. harvest is expected to exceed 12.5 million tons. California accounts for most of the U.S. production shown in Figure 1.

According to the U.S. Department of Agriculture, California's processing tomato production for 2007 was higher than expected due to very favorable weather. In contrast, poor weather plagued California tomato growers in 2006. The 2007 processing tomato crop in California is estimated to have exceeded 12.1 million short tons (about 11 million metric tons). The big crop is due to increased acreage and excellent yields (about 41 tons per acre). This season's crop is very close in volume to the record 1999 crop, which led to lower prices and doom and gloom in the industry at that time. But the underlying fundamentals are much different now, with abundant optimism regarding the economic prospects for the California industry. This is not to say that uncertainty does not characterize the near-term future of the industry. One major factor facing all of California agriculture right now is a potential shortage of irrigation water in 2008. Last winter was relatively dry in California and given the poor start to rainfall (and snow) this winter, the state water authority recently informed most water districts that they may only receive 25 percent of their normal allocations in 2008. In 2007 these districts were allocated 60 percent of their normal water supply. To complicate the situation, the courts have also ordered the reduction of water deliveries to the central and southern part of the state from the Sacramento-San Joaquin

Delta, to help save an endangered species of fish.

California's tomato growers are beginning to negotiate with processors for prices and acreage in 2008. The California Tomato Growers Association (CTGA) bargains on behalf of about 50 percent of the state's growers and the CTGA is asking for a price hike to \$70 per ton for the 2008 crop. This is up from \$63 last year and \$50 just a few years ago. In addition, the growers are asking processors to share the risk associated with any increase in water costs. The growers are clearly sending a message to the processors that the farmland has other alternatives, given that many other commodity prices are up for 2008. Negotiations over prices will play out over the next few months and there may well be fewer acres of processing tomatoes in 2008. However, it is doubtful that tomato acres will drop sharply for at least two reasons. First, over 30 percent of the processing capacity is owned by growers themselves and their acreage is virtually committed to tomatoes. Second, the other processors are looking at another profitable year and

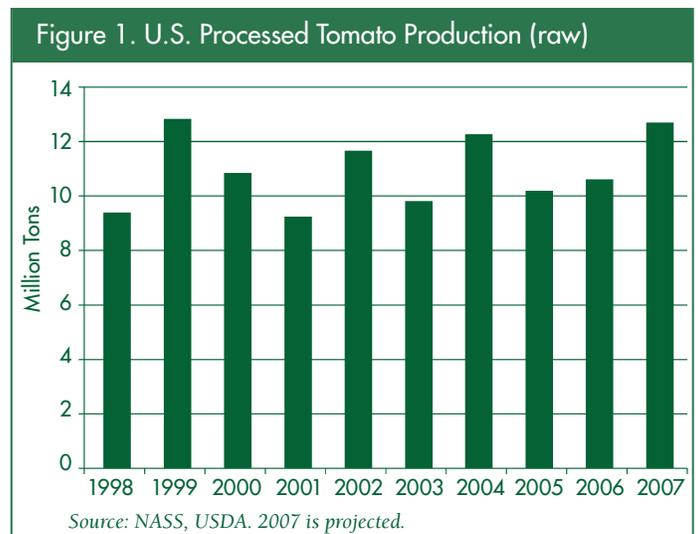
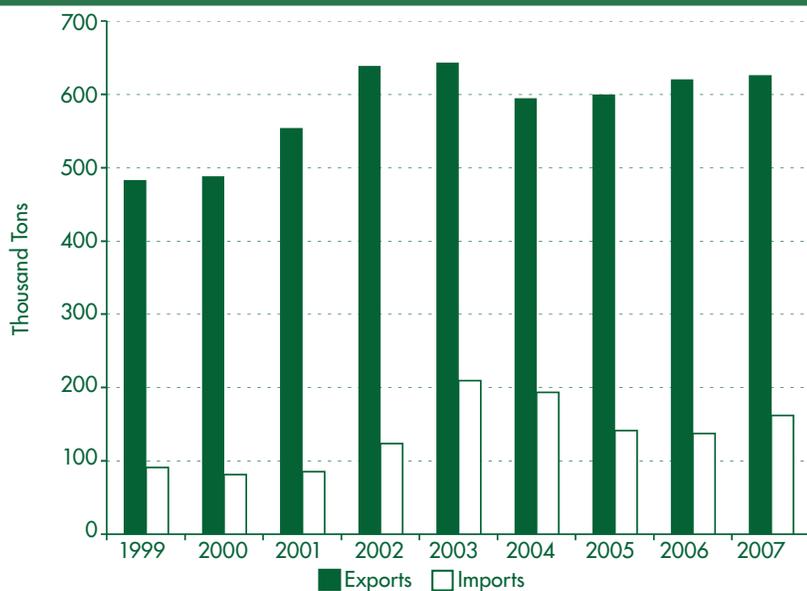
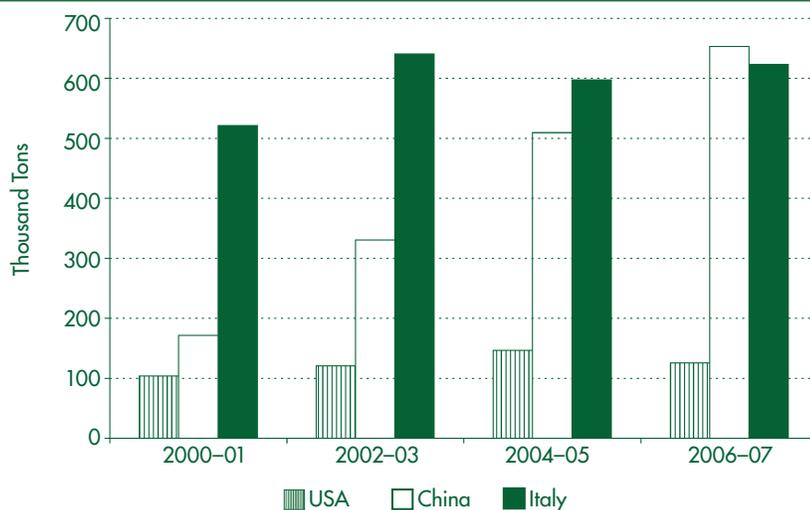


Figure 2. Italian Exports and Imports of Tomato Paste and Puree



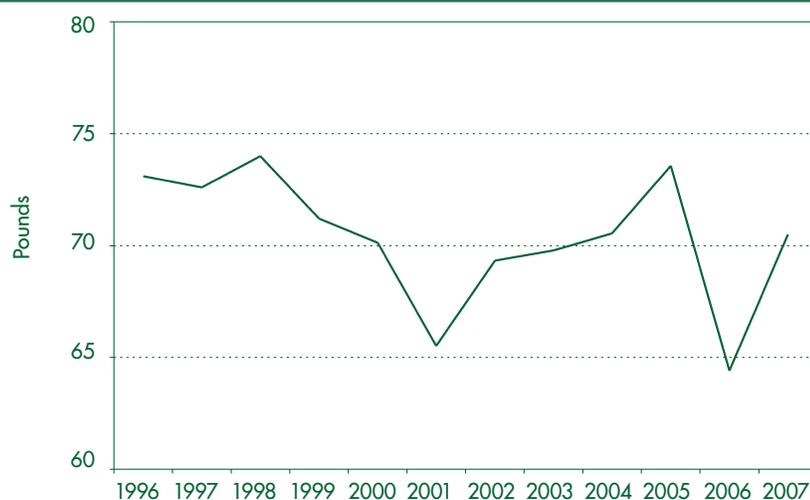
Source: Global Trade Atlas, July-June marketing year.

Figure 3. Tomato Paste and Puree Exports: Annual Average (July-June)



Note: Annual average based on a 2-year average. Source: Global Trade Atlas, July-June marketing year.

Figure 4. U.S. per Capita Consumption of Processing Tomatoes (lbs. farm weight)



Source: USDA, ERS

they are in a position to offer a good price to growers.

Apart from this uncertainty, which is not unusual, today's outlook for processing tomatoes is so much better than in 2000 largely due to strong international demand. Yes, California can effectively compete internationally in the tomato paste market. Of course, the lower valued U.S. dollar will also serve to boost California's international competitiveness in the coming months. The dollar peaked in value about five years ago, and since then it has lost about 25 percent of its value against a broad basket of currencies. However, the dollar's drop has been much steeper against the European euro. Since 2002, the euro/dollar exchange rate has fallen from 1.13 to 0.68 (euros/dollar)—roughly a 40 percent drop.

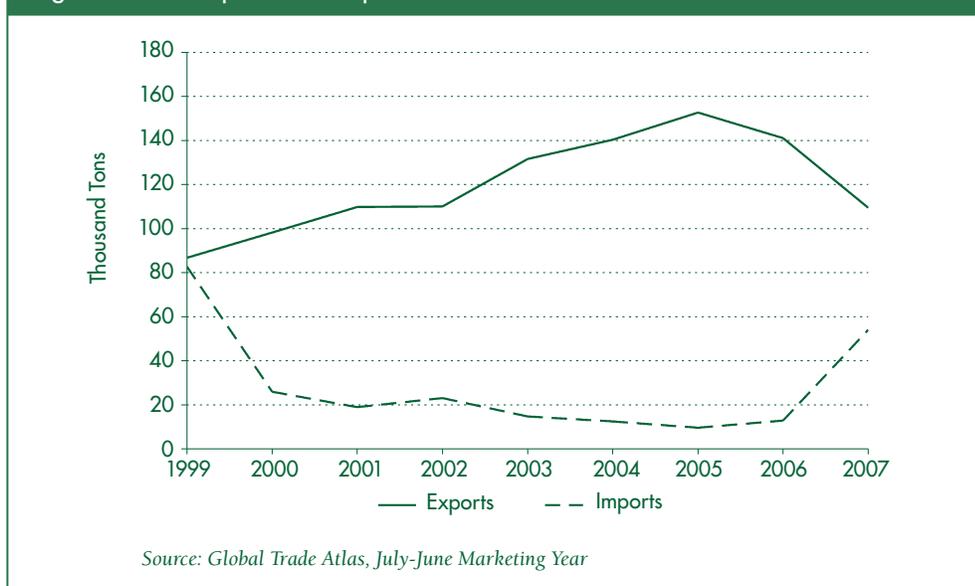
Taking a closer look at the international market for tomato paste, the large exporters are China, Italy, Spain, Portugal, the USA, Greece, Turkey, and Chile (in order of importance, based on the last three years). On the import side, the big players are Germany, Russia, Italy, the UK, Japan, France, Canada, and Mexico. Import demand growth has been exceptionally strong in some of these markets. For example, Mexico's tomato paste imports have tripled in the last four years and the volume of imports exceeded 89,000 tons in 2006-07. Russia, another big player in tomato paste, has expanded its imports by about 50 percent in the last four years, shipping in 149,000 tons in 2006-07.

Italy appears on both lists of top exporters and importers because there is a tremendous amount of intra-industry trade in tomato paste. The USA also imports and exports tomato paste, but not on the same scale as Italy. In the 2006-07 marketing year, Italy imported about 162 thousand tons of paste and puree, and at the same time exported about 626 thousand tons. In comparison, for that same year, the U.S. imported 54 thousand tons and

exported about 109 thousand tons of paste. Italy's intra-industry trade in tomato paste and puree is shown in Figure 2, for the 1998–1999, through 2006–2007 time period. Over the nine marketing years shown in Figure 2, on average, Italy exported about 583 thousand tons of tomato paste and imported 136 thousand tons. Interestingly, Italian imports in a given year exceed the total volume exported from the United States. The doubling of Italy's tomato paste imports over the time period shown in Figure 2 has allowed that country to boost its exports at the same time. China is the dominant source of Italy's imports, accounting for over 70 percent. Chinese paste is imported into Italy, repacked and/or further processed and re-exported. The Italian growers have convinced their government to erect import trade barriers against China's tomato products, but imports continue to flow despite these new trade barriers. For instance, in the past few years, Italy has tightened labeling regulations for tomato paste and introduced country-of-origin labeling that has served to discriminate against imports from China. This is bad news for Italian processors because they face a shortage of tomatoes in 2008 and beyond due to the ongoing decoupling of farm payments in the European Union—a farm policy move that is expected to lead to reduced processing tomato acreage in Italy and elsewhere in Europe.

Figure 3 displays the annual average paste and puree exports for the top three processing countries: the USA, Italy, and China. Each vertical bar in the figure represents annual average July–June exports (in thousands of tons) over a two-year period. The export boom enjoyed by China is really striking. Annual exports of paste from China averaged around 172 thousand tons in 2000–2001, and this increased by more than three and one-half times to reach 653 thousand tons in 2006 and 2007 (year ending in June), on average. From

Figure 5. U.S. Exports and Imports of Tomato Paste and Puree



July 2006–June 2007, China exported over 715 thousand tons of paste and puree, due to rapid expansion of the domestic industry and strong global demand. Most of China's processed tomatoes are produced in the north-west province of Xinjiang, but production is also growing in the neighboring Inner Mongolia region. Inner Mongolia is well situated to service the international market.

China's tomato paste exports are expected to be substantially lower this marketing year, due to smaller stocks coming into the 2007 harvest and serious plant disease problems in the Inner Mongolia region. Inner Mongolia accounts for about one-third of China's tomato crop and that northern region reportedly lost as much as 50 percent of its 2007 crop due to blight. This means that recent estimates for China's 2007 paste production are down from expectations.

Italy also experienced yield problems with the 2007 crop due to a hot summer and disease issues. The lighter crops in China and Italy will mean additional international demand for California tomato paste. To top things off for the California industry, U.S. domestic demand is also coming back and is expected to be up for the 2007

harvest. Figure 4 shows that U.S. per capita consumption has rebounded nicely to over 70 pounds per capita.

We see from Figure 5 that the gap between U.S. exports and imports was slowly widening over the last five or six years, until the poor harvest in 2006. In 2005, net exports reached 143 thousand tons. There is very good reason to believe that the gap between U.S. exports and imports (shown in Figure 5) will open again with the large 2007 harvest and strong overseas demand. Exports will likely balance a big production year for the California industry and carry-over at the end of this year is not expected to be burdensome, which means prices for paste should hold up. California is positioning itself to maintain a larger role in the international market in the years to come.

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