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Report Highlights:

Korea imported \$178 million of dairy products in 2003. It is expected that total imports in 2004 will reach \$200 million. Even though the U.S. has only an 18 percent market share by value, cheese products accounted for slightly more than half of all dairy imports from the U.S. and are expected to continue showing strong growth in the future.

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SECTION I. SITUATION AND OUTLOOK

Korea imported \$178 million of dairy products in 2003. It is expected that total imports in 2004 will reach \$200 million. Although the Korean economy is likely to remain one of the fastest growing economies among OECD nations, it is predicted that consumption will remain sluggish in the 2nd half of 2004 and in 2005.

Cheese imports from the U.S. reached \$13.8 million through the first eight months of 2004, an increase of 35 percent compared to last year. Even though the U.S. has only an 18 percent market share by value, cheese products accounted for slightly more than half of all dairy imports from the U.S. and are expected to continue showing strong growth in the future. U.S. cheese products are considered high quality compared to other competitors.

Whey imports from the U.S. were \$6.6 million, a seven percent increase compared to the first eight months of last year. The U.S market share in 2004 is expected to remain steady.

Imports of ice cream from the U.S. were \$1 million through the first eight months of 2004, a decrease of 53 percent. Imports from the U.S. took a major hit when Häagen Dazs started imported more French ice cream instead of U.S. ice cream.

Korea does not import raw milk, as there is currently a surplus in domestic production. However, limited domestic production facilities and unreliable local supplies will likely result in continued growth in imports of other dairy products.

Table 1: Major Dairy Products Import to Korea
(Metric Tons)

Products (HS Code)	Current Tariff	2002		2003		% Change	
		U.S.	Total	U.S.	Total	U.S.	Total
Cheese (0406)	36%	3,910	31,984	4,559	35,782	17%	12%
NFDM (0402.10)	(20% - 176%) ¹	0	4,150	0	4,554	0	10%
Whole Fat DM (0402.21)	(40% - 176%) ²	0	1,071	0	1,660	0	55%
Mixed Milk (0404.90)	36%	0	13,946	1	6,312	1%	- 55%
Butter (0405.10)	(40%- 89%) ³	20	1,000	11	1,255	-82%	26%
Whey Powder (0404.10.10)	(20% - 49.5%) ⁴	15,754	26,487	17,819	29,174	13%	10%
Ice Cream (2105)	54%	1,701	2,785	833	2,091	-51%	- 25%

Source: 2004 Korea Customs & Trade Institute

Notes:

1: 20% tariff within the quota of 1,034 metric tons, 176% tariff out of the quota

2: 40% tariff with the quota of 573 metric tons, 176% tariff out of the quota

3: 40% tariff within the quota of 420 metric tons, 89% tariff out of the quota

4: 20% tariff within the quota of 54,233 metric tons, 49.5% tariff out of the quota

Historically, Korea has produced a surplus of milk as consumption has relatively low. In order to assist the Ministry of Agriculture and Forestry (MAF) with this problem, a subsidiary

organization, the Korean Dairy Promotion Association (KDPA) was formed. Since 1999, dairy farmers have voluntarily paid one won (1,150₩=1\$) per kilogram of production to promote milk consumption. KDPA administers this fund to pay for television and radio commercials and other similar types of public relations and educational campaigns encouraging domestic consumers to drink milk. In addition, KDPA played a role in negotiating production and price levels between dairy farmers and the dairy industry.

However, the government and industry think that KDPA's role is not so relevant these days as the herd size has been sufficiently reduced and there has been a recent jump in dairy prices received by farmers. In addition, there is the Korean Dairy and Beef Farmers Association (KDBFA), which is also promoting dairy consumption. In the future, it is likely that KDPA will be dissolved and dairy farmers will work directly with the dairy industry in negotiating a price.

Table 2: Dairy Herd Information

	December 2002	March 2003	June 2003	September 2003	December 2003
Total Dairy Cows (% Change from 2002)	544,000	552,000	541,000	526,000	519,000 (-4.6%)
Milking Cows (% Change from 2002)	252,000	262,000	254,000	244,000	241,000 (-4.4%)
Dairy Farms (% Change from 2002)	11,700	11,700	11,300	10,800	10,500 (-10.3%)
Dairy Cows Per Farm	46.4	47	48	49	49

Source: 2004 Korea Livestock Yearbook

The European Union (EU), Australia and New Zealand are the main foreign competitors for U.S. product in Korea. The EU is price competitive in milk powder preparations, while Australia is a competitive cheese provider. Australian cheese is mainly imported in bulk and then processed by local Korean processors. Furthermore, the current trend for "slow food" is benefiting European products, which are viewed as products produced with great care as compared to "fast food" which are thought to be unhealthy.

Per capita consumption of dairy products decreased 3.4 percent in 2003 to 62.4 kilograms from 64.2 kilograms in 2002. However, the consumption of cheese and yogurt has shown positive growth in 2003, which is expected for the foreseeable future. The expanding younger generation (the under 20 crowd) and their penchant for western foods, such as pizzas, cheeseburgers and sandwiches, has been a boon to cheese sales. Koreans also believe drinking yogurt aids digestion problems, resulting in many people drinking yogurt, especially probiotic yogurt every day.

The current "well-being" trend emphasizes the consumption of healthy foods or functional foods--everyday items that can claim a health benefit, such as functional ice cream with ingredients such as aloe, black beans, black sesame or vitamins--are being introduced. Green tea milk and black bean milk are other examples of popular functional dairy foods. Green tea is known to prevent hypertension, sclerosis of the arteries and diabetes.

The popularity of soymilk has also grown dramatically as Korean consumers increasingly regard this drink as a health food and an alternative to dairy milk. Koreans believe milk

made from soy is better than regular cows' milk because it contains less fat and provides other minerals not found in regular milk. In addition, many Koreans are lactose intolerant.

1. Fluid Milk

In 2003, Korean raw milk production was 2.4 million metric tons, 6.7 percent down from the previous year, and is expected to steadily decline in the foreseeable future as the government begins to decrease support and the number of milking cows declines. However, drinkable (pasteurized) milk consumption increased by 10 percent, this category includes regular white milk and flavored milks. Regular white milk is becoming less popular than flavored milks and increased only 1.3 percent in the past year. In contrast, because of the popularity of flavored milks, such as black bean milk, overall processed fluid milk consumption has increased by 43 percent.

Out of total production, 1.6 million metric tons (69 percent) is for drinking use and 654,000 metric tons (28 percent) was processed. The remaining surplus of 76,000 metric tons (3 percent) was used for the production of whole and nonfat dry milk, which is then stored. Despite this surplus, Korea still needs to import milk powder. The price for local raw milk is about double the price of imported milk powder.

The following table shows the MAF's official estimates for milk production and consumption.

Table 3: Overall Milk Supply and Demand
(Thousand Metric Tons)

Year	Supply			Demand	Self Sufficiency	NFDM Inventory
	Production	Import	Total			
1998	2,027	282	2,309	2,299	88.2%	8.3
1999	2,244	456	2,700	2,752	81.5%	3.6
2000	2,253	640	2,893	2,807	80.2%	10.7
2001	2,339	653	2,992	3,046	76.8%	5.8
2002	2,537	646	3,183	3,060	82.9%	13.6
2003	2,366	604	2,970	3,037	77.9	7.9

Source: 2004 Korea Livestock Yearbook published by the Agriculture Fishery & Livestock Newspaper
Note: All dairy products were converted into raw milk equivalent units.

A growing niche market in Korea for beverages is that of specialty milk: milk with added nutrition, such as black beans, fruit flavored, soymilk, calcium, iron or vitamins. The consumption of these niche milk products has been growing at the rate of 10 percent per year.

2. Cheese

Total imports of cheese products were \$94 million (35,782 metric tons) in 2003, a increase of 11 percent from the previous year. Imports of cheese products in 2005 are forecast to reach 45,000 metric tons.

In 2004, total cheese imports are expected to increase 15 percent due to the lack of domestic production facilities and the increase in consumer demand for more and a wider variety of cheese products. The changing tastes of younger consumers and the continuing growth in fast food and "family style" restaurants, and the rapid growth of wine consumption, are expected to contribute to the increase in demand for a wide variety of cheese products. The Korean wine market increased by 60 percent in 2003, which is likely to result in increased consumption of new to market and high quality cheeses.

Local cheese production is constrained by the lack of manufacturing facilities. In September 2004, however, one of the leading dairy companies, Maeil Dairy, established a new natural cheese manufacturing plant in a joint venture with German Alphma Company, using manufacturing techniques acquired from New Zealand and Japan. The purpose of this new plant is to utilize the surplus local raw milk to make cheese. It is not, however, expected to impact demand for imported cheese in the near future.

While imports of U.S. cheese are benefiting from the general increase in cheese consumption, there is strong competition from Australia and New Zealand. The average price of imported U.S. cheese (\$3.75/kg) was \$1.13 higher than that for competitor products. Despite this difference, U.S. cheese has a good reputation among Korean consumers for taste and quality.

3. Nonfat Dry Milk (NFDM)

Imports of NFDM are forecast to increase 10 percent in the latter half of 2004 and 2005 because there has been a 13 percent increase in the raw milk price since September 2004 and the amount of surplus raw milk for locally produced NFDM has decreased. The retail price of locally manufactured NFDM is \$3.50 - \$3.90 per kilogram, an increase of 75 percent over last year, due to the current shortage of NFDM. The manufacturing cost is \$6 per kilogram.

There is an import quota of 1,034 metric tons for NFDM. The within quota tariff is 20 percent and the out of the quota tariff is 176 percent. From January to July 2004, imports of NFDM were 2,100 metric tons, an 11 percent decrease compared to last year. The average cost from the EU, Australia and New Zealand was \$1.86 per kilogram, CIF value.

Local food processors import NFDM for the purpose of re-exporting to other countries, including Saudi Arabia, Taiwan, China and Bangladesh, after having processed it into infant formula. The Korea Customs Service reimburses the high out-of-quota tariff of 176 percent to importers when they have re-exported the processed dairy-based products made from the imported NFDM.

Most NFDM is imported from Australia, New Zealand and the EU. There were no imports from the United States in 2003, nor to date in 2004. Importers complain that the U.S. price is too high.

The continuing decline in Korea's birth rate and the increasing popularity of breast feeding is leading to a decline in local infant formula consumption. Domestic infant formula sales have

remained the same over the past two years. Last year's birth rate was 1.17, with only 470,000 babies born per year for the past 2-3 years, which is the lowest birthrate in the world. The Korean infant formula market is static and the retail market price for domestic premium product is over \$16.50 (19,000 Korean Won) per 800 grams.

4. Other Dairy Products

Ice Cream

In 2004, the ice cream market in Korea, including functional ice cream, is expected to grow 10 percent. Functional ice cream is low fat, low sugar and green tea ice cream, and targets adults as well as teenagers interested in health and beauty. In 2003, the ice cream market recorded \$715 million (858 billion Korean Won) in sales. The sales of functional ice cream accounted for \$7.2 million (8.6 billion Korean Won), about 1 percent of the total market.

Because ice cream imports grew at an average annual rate of about 20 percent in the past six years, it was anticipated that the trend would continue at a rate of 10-20 percent in the next five years. However, the largest importer, Häagen Dazs, since 2002, has used ice cream manufactured in France, instead of the U.S., for export to Korea. This switch resulted in the U.S. market share dropping from 60 percent in 2002 to 34 percent in 2003. Additionally, the Dippin & Dots Ice Cream Company and the Mini Melts Company are now manufacturing their ice cream (starting in 2002) locally. Consequently, the U.S. market share has dropped further to 22 percent so far in 2004 (Jan-Aug) and it is expected to continue to decline.

The Korean ice cream market is dominated by four Korean ice cream manufacturing companies, Lotte, Bingrae, Haitai, Samkang, which accounted for 90 percent of the whole ice cream market in 2003. Out of the remaining 10 percent, leading premium foreign ice cream companies such as, Baskin Robins and Dippin Dots (locally produced with imported ingredients) accounted for 7 percent. Other major premium imported brands include Blue Bunny, Ben & Jerry's and Aggie.

The ice cream market has been slow this year, despite the warm summer weather, due to the sluggish economy.

Whey Powder

Whey powder imports are forecast to increase 15 percent by volume in 2004 as there are not enough local facilities to produce the whey powder to meet local demand. Imported whey powder costs an average of \$0.42 per kilogram on a CIF basis. Imports of whey powder should continue to increase.

Imports of whey powder (HS 0404-10-1010) were \$12 million (29,174 metric ton) in 2003, increased by 10 percent from 26,487 metric ton in 2002. Seventy percent of imported whey powder is utilized for animal feed. In 2003, \$7.6 million (17,819 metric ton) was imported from U.S. with a market share of 61 percent. The major foreign competitor for the U.S. is France.

Table 4: Imports of Whey in 2003

Products (HS Code)	Volume (Metric Tons)		Value (U.S. Dollars)	
	Total Imports	Imports from U.S.	Total Imports	Imports from U.S.
Whey Powder (0404-10-1010)	29,174	17,819	12,213,764	7,624,726
Other (0404-10-1090)	3	0	21,736	0
Demineralized Whey (0404-10-2120)	5,422	8	5,685,828	52,370
WPC (0404-10-2130)	1,399	731	3,804,940	1,933,994
Other (0404-10-2190)	3,355	2,286	2,574,759	1,129,656
Other Mixed Milk Powder (0404-90-0000)	6,312	1	12,696,132	63,119
TOTAL (0404)	45,665	20,845	36,997,159	10,803,865

SECTION II. STATISTICAL TABLES