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Report Highlights:

Large-scale restaurants under franchise operation and broad-line distributors are rapidly growing at the expense of small-scale, family-owned businesses. There is an increased emphasis on products with new tastes, added value, stable pricing and volume capability, and products with specifications geared specifically for the food service industry. As a result, the demand for imported products is growing.

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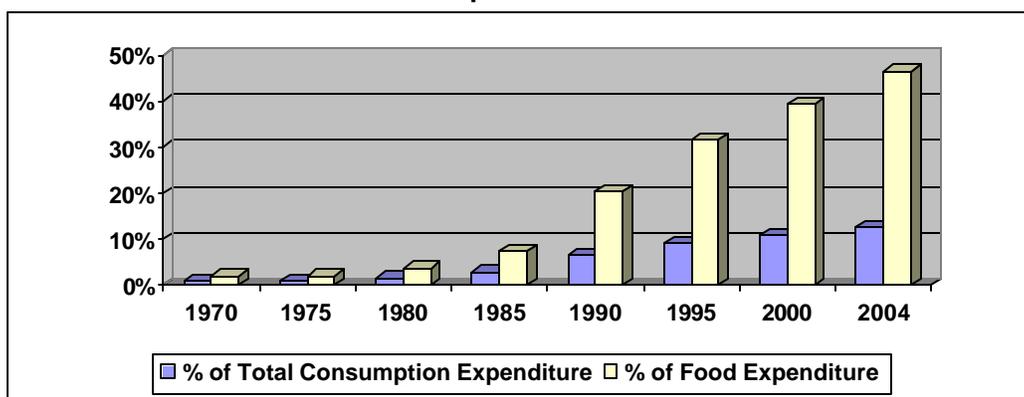
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Section I. Market Summary

A. Executive Summary

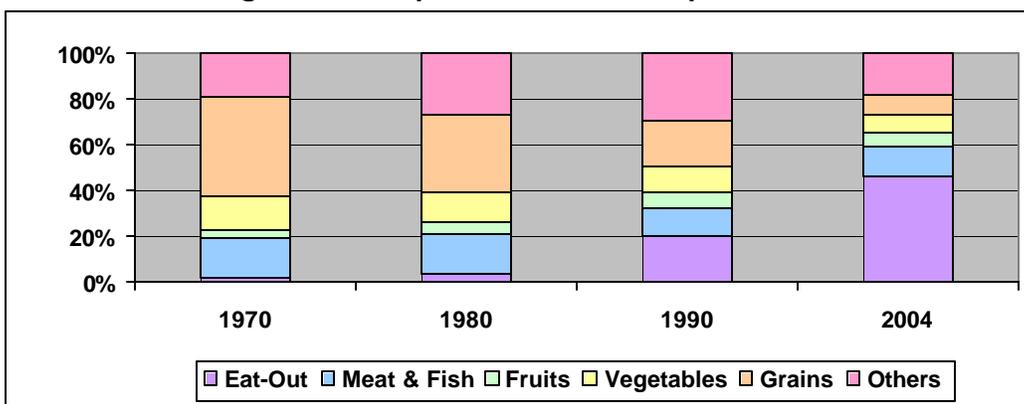
Changes in lifestyle and dietary culture coupled with increased consumer income have led to a rapid growth of the food service sector in Korea. Monthly average per capita spending on eating outside of the home has continued to rise, reaching a record high of 75,535 won¹ in the third quarter of 2005, up one percent from the year before. In other words, each Korean spent 45 percent of his/her food expenditure, or 12.1 percent of their total consumption expenditure, dining out. The share of eating-out, relative to both food expenditure and total consumption expenditure, has consistently increased and this trend is expected to continue in the years to come.

Figure 1. Share of Eating-out Relative to Food Expenditure and Total Consumption Expenditure



Source: Korean Government Statistics (Jan. 2006)

Figure 2. Composition of Food Expenditure



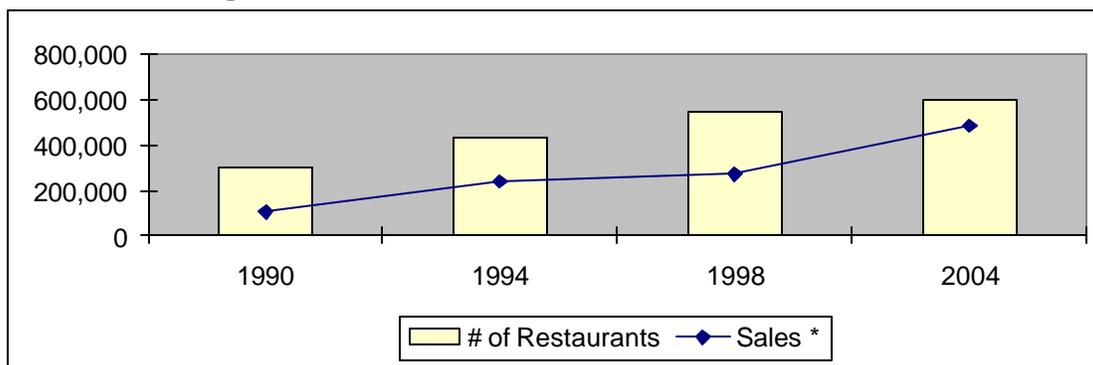
Source: Korean Government Statistics (Jan. 2006)

The Korean food service sector earned a record high of ₩48.4 trillion of cash register sales in 2004, up 9.3 percent from the previous year. Even though the sector is expected to continue grow at a robust rate, it is widely believed among market analysts that the sector has come to a saturation point in terms of the total number of restaurants, as indicated by a negative growth in the number, for the first time in history, from 605,614 to 600,233 in 2004. The restaurant industry has been a major refuge to many of those people who lost their

¹ US \$1 = 980 Korean won (₩) as of January 31, 2006.

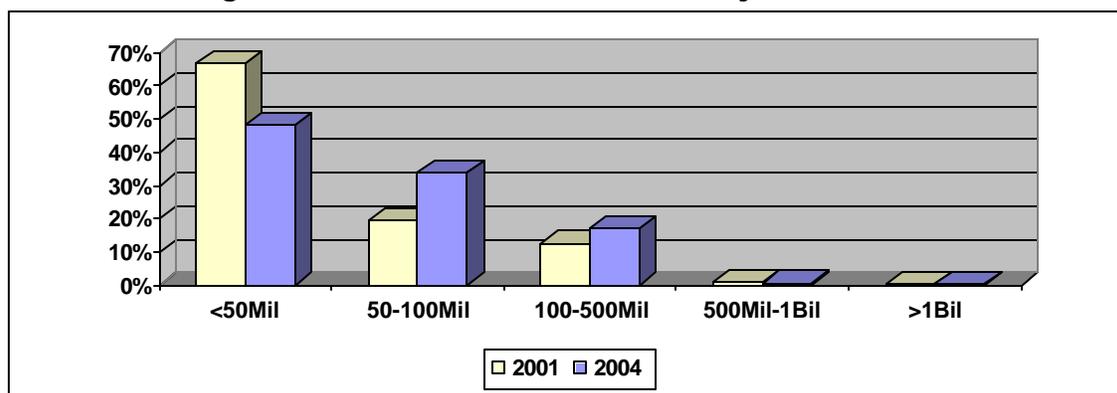
corporate jobs during and aftermath of the Asian economic crisis in the late 1990's. In addition, entry into the restaurant business was previously allowed by law only to individuals and small businesses up until the mid 1990's. As a result, most restaurants were small scale, family-owned businesses, as shown by the government statistics that 91 percent of restaurants in Korea were small family-owned businesses that hired less than five employees in 2004. In addition, about 48 percent of restaurants made less than ₩50 million in annual cash register sales.

Figure 3: Number and Annual Sales of Restaurants



* Note: Annual cash register sales in ₩100 million
 Source: Korean government statistics (Jan. 2006)

Figure 4: Breakdown of Restaurants by Annual Sales



Unit: Korean won
 Source: Korean Government Statistics (Jan. 2006)

Restructuring, fueled by increasing competition, government deregulation and the on-going economic slowdown, has led to a rapid growth of large-scale restaurants under chain or franchise management of various formats, including full-service family restaurants, quick-service fast food restaurants, bars, and institutional restaurants, at the expense of small-scale family-owned establishments. At the same time, consumers' increasing demand for new and international tastes has resulted in a diversification of the sector with new-to-market products, recipes and restaurant concepts.

Streamlining of the supply chain is another area in which the sector has made significant progress in recent years. 'One-stop, broad-line' distribution services are rapidly growing, as several conglomerates are making heavy investments in the market, competing against traditional multi-layered supply channels comprised of independent wholesalers and wet markets.

The rapid growth of large-scale businesses, in both restaurant operation and product distribution, is resulting in increased demand for products with new tastes, stable pricing and volume capability, added-value, and specifications catered to the food service sector, characteristics where U.S. products are competitive. U.S. products are particularly likely to maintain a strong market share in the thriving premium restaurant segment in the coming years. The outlook for U.S. exports is excellent for beef, pork, poultry products, seafood, processed vegetables, fruits, nuts, dairies, juices, alcohol beverages, sauces, condiments, cooking oils, organic foods, coffee and frozen desserts. In addition, on-going trade liberalization will generate further export volume to those products that are currently under restrictive import barriers in the form of tariffs, volume quotas and food safety regulations.

B. Advantages and Challenges for U.S. Exports

Advantages	Challenges
1. The Korean market is a growing market where new ideas and trends are eagerly tried and accepted, leading to greater opportunities for new-to-market products.	1. Many consumers maintain a negative view on the quality and safety of imported foods. Imported foods are often associated with contaminations and potential food-borne diseases. In addition, food safety issues are increasingly becoming a means to restrict imports.
2. Consumers are looking for new and international tastes. Korean consumers are very familiar with American style menus and restaurant concepts.	2. Many products, such as fresh potatoes, honey and apples, have limited market access due to quotas, high tariffs and SPS issues.
3. Large-scale businesses are leading the growth in the sector.	3. Although changing, price is still the most important factor in procurement decisions. Unfortunately, few decision makers understand the overall benefit of using higher quality, value-added products.
4. On-going lifting of import barriers improves the market accessibility and price competitiveness of imported U.S. products. This will be especially true in the coming year as Korea and the United States begin to develop a free trade agreement.	4. Many U.S. products are similar to those from export-oriented countries, such as China, Australia, Thailand and New Zealand, and face serious competition.
5. On-going depreciation of the U.S. dollar against international currencies, including the Korean won, makes U.S. products more price-competitive.	5. U.S. suppliers often find it difficult to supply customized products required by Korean food service buyers mainly because either the ordered volume is too small to justify the needed changes in the manufacturing process, labeling, etc.; or the supplier has little understanding about Korean recipes and may not know how to meet the specifications.

Section II. Road Map for Market Entry

A. Entry Strategy

The following is a list of key components of a market entry strategy that has been proven effective for new-to-market suppliers:

- Locate and work with an established importer who has an effective sales, marketing and distribution network focused on target customers.
- Research and develop products that meet consumer tastes and current trends, including making changes to existing recipes and specifications.
- Sell recipe ideas first, not products.
- Maintain price competitiveness either by trading in a large volume or adding value to the product. For example, consider offering processed products, such as pre-marinated chicken instead of a raw product so that the restaurant can save labor and kitchen preparation costs.
- Keep abreast of and respond quickly to changes in the supply and demand situation in the market.

Any U.S. supplier seeking opportunities in the Korean food service sector first needs to understand the sector's specific needs.

Understanding Local Tastes:

Dishes served in Korea largely reflect the contemporary dietary culture of Koreans and, even though ethnic food is gaining in popularity, almost all of these dishes are developed with local tastes in mind. Considering the rapid evolution of the sector, it is also important to be kept informed of the changing tastes of Korean consumers to stay ahead of the competition. A rule of thumb is that new food trends in Korea are two to five years behind Japan, although the time gap looks getting narrower over the years. In addition, even products that are used in similar dishes in the United States may require different specification. Meeting the sector's specific needs could mean anything from modifying cuts, reducing portion sizes, changing the saltiness, adding or deleting some ingredients.

Local Representation:

Because of the many variables involved, there is no one best way to enter the Korean market. Success is unlikely, however, without proper local representation and catered attention. What form this local representation takes depends on the nature of the exporter, the product, and the local distribution channel. Unless the U.S. supplier has a specific position on this, working with an established broad-line importer on a commission basis during the initial stages of market entry is highly recommended. Established importers are well aware of up-to-date market demand/supply intelligence, business practices, local business laws, distribution channels, and, most of all, are the best source of current information on government labeling and inspection regulations for imported foods². ATO Seoul also maintains listings of local importers by product, which are available to U.S. suppliers upon request at no cost. Exhibiting in a local food trade show is a cost-efficient way to meet with a large number of key traders in the sector. Currently, the Food & Hotel Korea (FHK) is the only local show endorsed and supported by U.S. Department of

² A brief report on the Korean government's regulations for imported food products (FAIRS Report) can be found in the ATO Seoul website (www.atoseoul.com) or USDA/FAS website (www.fas.usda.gov). Exporter Guide to Korea, written by ATO Seoul annually, is highly recommended to new-to-market exporters who are seeking guidance about entering the Korean market. Additional reports on products and market sectors are available from these websites.

Agriculture/Foreign Agricultural Service (FAS)³. Exporters who are considering exhibiting at other shows should contact the ATO for more information about the particular show they are interested in. Most local trade shows are consumer-oriented, which is not particularly useful for promoting new-to-market products.

Franchises:

Many of the leading restaurant chains in Korea are of U.S. origin and can be approached through the headquarters in the United States. The degree of involvement of the U.S. headquarters in the operation of the partner chains in Korea varies from one company to another depending on the nature of the contract between them. U.S. headquarters in general have a significant amount of influence over what products and recipes the Korean partners will incorporate. Below is a list of U.S. origin restaurants currently in operation in Korea.

Table 1: A List of U.S. Origin Restaurants in Korea (2006)

Segment	Chains
Fast Food Restaurants	McDonald's, KFC, Burger King, Subway, Popeye's
Family Restaurants	TGIF, Bennigans, Outback Steakhouse, Sizzler, Chili's, Toni Roma's, Ruby Tuesday, Hard Rock Cafe
Ice Cream Restaurants	Ben & Jerry's, Haagen-Dazs, Cold Stone Creamery, Baskin Robbins
Pizza Restaurants	Pizza Hut, Domino Pizza, Papa John's
Coffee & Deli Shops	Starbuck's, Seattle's Best, Au Bon Pain, Krispi Kreme Doughnuts, Cinnamon, Dunkin Doughnuts

B. Market Structure - Distribution Channel

Traditional Distributors:

Most of independent, family-owned restaurants still procure products on their own from traditional distribution channels, which include multiple layers of wholesalers and wet-markets. Wholesalers and wet-markets in general are specialized by certain product categories and are considered the best source of fresh food at a good value. However, sales of these traditional channels are on a gradual decline just like their customers, as they face tougher competition against mass-volume, one-stop service distributors. In addition, strengthened government tax regulation has deteriorated price competitiveness of traditional distributors who in the past were given a large amount of tax breaks.

Broad-line Distributors:

The rapid growth of large-scale restaurants is prompting an equally rapid growth of broad-line, one-stop service mass-distributors. Currently, about five large local conglomerate businesses, all committed to becoming the "Sysco of Korea" someday, operating nationwide distribution networks with modern temperature-controlled warehouses and truck fleets. They supply a wide variety of products mainly to large-scale restaurant chains and hotels; however, these broad-line distributors are currently focusing mainly on high-volume products and, thus, have not yet become 100 percent capable of 'one-stop' service. Consequently, restaurants that use broad-line distributors also procure from a multiple number of specialty suppliers concentrating on low-volume, high-value products. Below is a brief description of the way products are procured by local broad-line distributors:

³ Detailed information about this trade-only show can be found in its website (www.fhko.com).

- Long-storage agricultural products (such as onions, dried pepper, carrots and potatoes) are procured from local contract farms and/or from the National Federation of Agricultural Cooperatives (NACF).
- Fresh vegetables are procured from local contract farms, usually large-scale green houses that supply fresh products around the year.
- Fresh vegetables subject to seasonal supply fluctuations (such as Chinese cabbage and radish) are procured locally through middlemen in the wholesale auction market.
- Local meat is procured through local middlemen in the wholesale meat auction market.
- Locally processed vegetables (frozen, canned and pickled) are procured from domestic manufacturers every one to three months through price bidding.
- Locally processed foods (such as oils and sauces) are procured from domestic manufacturers on a yearly contract.

In general, broad-line distributors operate processing facilities attached to their warehouses for preliminary processing of vegetables and meat, such as washing, cutting, repackaging and limited cooking. Some of the leading companies also operate food manufacturing facilities and make private branded processed products, such as soups, sauces and packaged marinated meat.

Imported food products of all types are procured from importers or, to a lesser extent, directly from overseas suppliers. Broad-line distributors prefer to import directly from overseas suppliers for high-volume products, such as meat, seafood and canned vegetables, while preferring to use middlemen importers for low-volume or products of seasonal demand.

Imports and distribution of products under import quota restrictions, including fresh potatoes, onions, grains and honey, are handled by the Korea Agro-Fisheries Trade Corporation (aT), formally known as the Agri-Fishery Marketing Corporation (AFMC). aT is a government agency within the Ministry of Agriculture and Forestry (MAF). In general, the set annual import quota is divided evenly among the importers who signed up for the product. In other cases, the quota is allocated to importers through auction. A broad-line distributor may acquire an import quota allocation or purchase from other importers who acquired an allocation.

Table 2: A List of Broad-line Food Service Distributors (2004)

Company Name	Annual Distribution Volume (Estimates) ^{1*}	Web-site
CJ Food System	₩450 billion	www.cjfood.com/eng
Our Home Co.	₩150 billion	www.ourhome.co.kr
Samsung Everland	₩120 billion	www.samsungeverland.com/eng
Foodmerce	₩100 billion	www.foodmerce.com
KTSC ^{2**}	₩130 billion	www.ktsc.co.kr
Hyundai Food System	₩ 70 billion	www.hyundaifoodsystem.com

* Notes:

1/ Sales of food service distribution division only

2/ Korea Tourist Supply Center Co., Ltd.

Source: Korea Food Distribution Yearbook 2005, Industry Sources

Food Processors:

The local food processing industry is the major supplier of processed products to the food service sector. Although food processors in general mainly focus on retail products, more and more are shifting attention to the food service sector in order to capitalize on the rapid growth within this sector. Many processors have developed strategic alliances with broad-line distributors to market food service products under the distributor's brand name. While a large portion of these co-packed products are simply the same retail products in bigger volume packages, some are developed exclusively for the food service market. CJ, Daesang, Ottogi and Dongwon are the leading players in this area. Although products by local processors are currently limited to big volume items, it is expected that processors will expand into more diverse products in the coming years, many of which will compete directly with imported consumer-ready products. Local processors, however, will be more dependent on imported ingredients. Products from local processors are generally distributed through multiple layers of wholesalers or regular retail stores before reaching end users unless they are bound directly for broad-line distributors.

Discount Retail Stores:

Discount retailers, supermarkets and membership warehouse clubs are an important distribution channel for the food service sector, as many small-scale, family-owned restaurants procure products there. Currently, there are about 300 mass-volume discount stores nationwide, to which about a dozen new stores are expected to join every year. E - Mart, a local chain, is the leading player, while four international chains, Carrefour, Wal-Mart, Tesco and Costco are closely following behind. In particular, Costco has been the most active in targeting small-scale independent restaurants.

Development of the modern food service distribution system in Korea is an outcome of on-going market liberalization. Imports and distribution of food products to the food service sector were under a monopoly system up until the early 1990's. It was not until the early 1990's that conglomerate businesses were allowed to enter this sector. These companies are now the key reason behind the outstanding growth of chain and franchise restaurants, as well as broad-line food service distribution.

C. Sub-Sector Profiles**1. Hotel Segment****Table 3: Lodging Industry Market Share (2001^{1*})**

	Number of Business	Number of Room	Cash Register Sale
Hotels	1.8%	10.1%	68.0%
Inns	78.5%	77.6%	23.1%
Resort Condos	0.3%	4.3%	6.1%
Others	19.4%	8.0%	2.8%
Total	34,317	584,304 rooms	₩6,545,113 million

* Note: 1/ Year 2001 is the most recent year for which data is available.

Source: Korean government statistics 2004

Table 4: Hotel Segment Statistics Broken Down by Number of Rooms

Category: Number of Rooms	<50	50-100	100-300	>300	Total	
Number of	2004	163	232	114	42	551

hotels	1999	332	276	118	25	751
	Change	-103.68%	-18.97%	-3.51%	40.48%	-36.30%
Number of employees	2004	2,438	6,812	12,539	18,931	40,720
	1999	4,431	9,659	14,317	10,591	38,998
	Change	-44.98%	-29.48%	-12.42%	78.75%	4.42%
Cash register sales ^{1*}	2004	95,419	316,176	766,697	2,258,143	3,436,435
	1999	155,076	373,573	716,976	831,143	2,076,768
	Change	-38.47%	-15.36%	6.93%	171.69%	65.47%
Room sales ^{1*}	2004	40,445	149,967	331,407	720,525	1,242,344
	1999	56,855	159,171	253,220	196,538	665,784
	Change	-28.86%	-5.78%	30.88%	266.61%	86.60%
Number of rooms	2004	6,320	15,326	17,846	20,865	60,357
	1999	12,484	17,745	18,020	10,637	58,886
	Change	-49.38%	-13.63%	-0.97%	96.15%	2.50%
Number of guests ^{2**}	2000	5,037,564	7,650,031	8,776,468	9,892,972	31,357,035

* Notes:

1/ Unit in million won

2/ Year 2000 is the most recent year for which data is available.

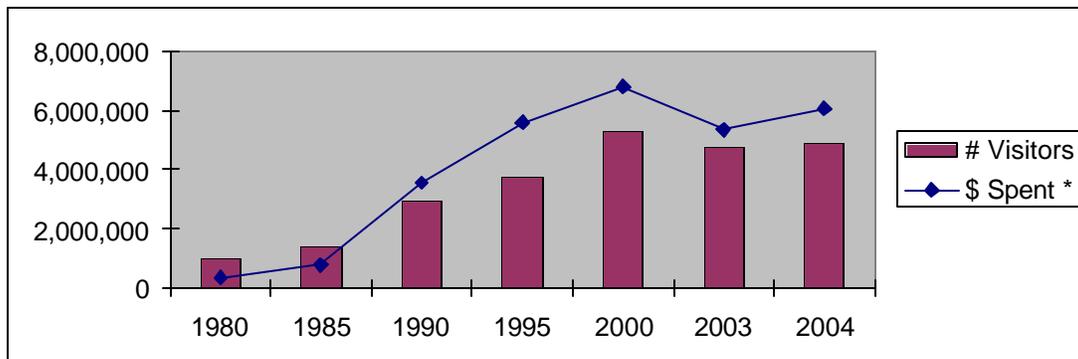
Source: Korean government statistics (Jan. 2006)

There were 551 hotels in Korea at the end of 2004, 200 less than five years before. This significant drop was mainly caused by a decrease in the number of small-scale hotels with less than 50 guestrooms. However, the growth of large-scale hotels over the past several years has more than compensated for the loss, resulting in outstanding growth of cash register sales of the sector, which earned ₩3.44 trillion of cash register sales in 2004, up 52 percent from 1999. Compared to 2003, there was an increase of 16 hotels and an 8.9 percent increase in hotel sales during 2004. The hotel segment is estimated to comprise about 52 percent of total lodging industry sales in Korea. Another 48 percent of industry sales is shared by 30,000 inns and 6,000 resort condos and recreational facilities.

Competition has precipitated the restructuring of the industry, favoring the steady expansion of large-scale hotels at the expense of independent small-scale hotels. In 2005, the first six-star hotels opened: W Hotel by Starwood Hotels & Resorts World Wide Inc. and the Park Hyatt Seoul. As five-star hotels expand both in and outside of Seoul, many four-star hotels have joined professional management franchises, such as Hyatt, Ramada and Marriott, to remain competitive in price and operational efficiency. Middle-sized hotels have gone under the umbrella of budget-format franchises, such as Best Western, Day's Inn, Ramada Inn and Holiday Inn, targeting the niche market of low-budget tourists and business travelers. The rapid growth of untraditional lodging formats, in particular service residences, pension homes, by-the-hour motels and hot-spa houses, has also resulted in the closing of many small-scale hotels and inns. These trends indicate that the diversification of the local lodging industry will continue in the years to come.

The hotel segment is expected to maintain a healthy growth in the coming years both from domestic and international travelers. In particular, the five-work-day system, which became a national standard for most Korean workers in the mid-2005, is expected to significantly boost up domestic tourism. A steady growth in the number of foreign travelers to Korea is also anticipated in the coming years.

Figure 5: Foreign Travelers Visiting Korea



* Note: Unit \$1,000

Source: Korean government statistics (Jan. 2006)

A good number of new hotels are currently under construction or are planned in order to meet the increased demand for additional hotel rooms. According to a government study, the market will need an additional 16,000 guestrooms by 2010 in the Seoul metropolitan area alone. Among others, a hotel belt in Goyang-city, a satellite town of Seoul, is currently under development by the government to meet this need. The shortage of hotel rooms is expected to be worse in regional markets where new industrial or tourist districts are under development. Recognizing the emerging opportunities, local conglomerates have unveiled plans for new hotels. A 106 story hotel currently under construction by Lotte Hotel in Busan, which, upon completion, will be the tallest hotel building in the world, is an example of investments being made in the sector.

The hotel sector, especially five and four-star hotels with in-house premium restaurants, has played a leading role in introducing new-to-market food products and recipes to local opinion leaders. It also has served as an efficient venue for promotional activities, including menu promotions, product launchings and technical seminars. Currently, food and beverage sales are estimated to comprise 40-50 percent of total sales in five and four-star hotels. Some leading hotels, including the Shilla and the Westin Chosun, have expanded their food service businesses outside of their hotels and now operate stand-alone food outlets of various formats, including microbrew pubs, food courts, coffee shops, bakery shops and premium gourmet restaurants. Although the role played by hotels in the food service sector is comparatively on a gradual decline due to the growth of restaurants on the street, it is likely that the sector will remain a leading distribution channel for premium, high-quality imported food and beverage products.

2. Restaurant Segment

Table 5: A Brief History of the Restaurant Industry in Korea

Year	GNP ¹ *	Major Events
1900	N/A	? Birth of the modern commercial restaurant industry.
-		? A total of 166 restaurants in business in Korea as of 1945.

1950's		
1960's	\$100 - \$210	? Most consumers had very low income and limited food supply. ? Western foods, mainly wheat flour and dried milk, first introduced to the public through the food aid programs by the United Nations and the United States.
1970's	\$248 - \$1,644	? A large number of small mom-and-pop restaurants opened in metropolitan cities. ? Rapid improvement in the diet of the general public due to economic development. ? Opening of the first franchise restaurant chain, Nandarang (1979) and the first fast food restaurant chain, Lotteria (1979). ? Imported foods first become available commercially to hotels with the establishment of the Korea Tourist Supply Center (KTSC), a monopoly import distribution agency (1978)
1980 - 1985	\$1,592 - \$2,158	? A limited variety of Western menus penetrated to the general public. ? The rapid expansion of franchise restaurants (mainly hamburger, noodle, fried chicken, and draft beer pubs). ? The first wave of international restaurant chains entered the market: Americana (1980), Burger King (1982), Wendy's (1984), KFC (1984), Pizza Hut (1984), Baskin Robbin's (1985).
1986 - 1990	\$2,194 - \$4,197	? The Asian Games in 1986 and the Olympic Games in 1988, both held in Seoul, introduced a wide variety of international recipes to the market. ? Rapid development of restaurants and bars under western themes. ? Introduction of the institutional food service business: Seoul Catering (1989), Our Home/LG Mart (1989). ? More international restaurants entered the Korea market: McDonald's (1986), Denny's (1987), Pizza Inn (1988), Cocos (1988), Crown Bakery (1988), Chicago Pizza (1988), Domino's Pizza (1989).
1990's	\$5,883 - \$10,076	? Conglomerates allowed to enter the food service business. ? Diversification of food service industry with new formats and menus. ? Hardies (1990), TGIF (1991), Haagen-Dazs (1991), Subway (1992), Ponderosa (1992), Sizzler (1993), Mister Pizza (1993), Sky Lark (1994), Kenny Rogers (1994), Popeye's (1994), LA Farms (1994), Bennigan's (1995), Tony Roma's (1995), Planet Hollywood (1995), Marché (1996), Hard Rock Café (1996), Outback Steak (1997), Chili's (1997).
2000's	\$10,000 - \$14,100 ^{2**}	? Restaurants under chain or franchise management led the growth of the sector at the expense of small scale, independent restaurants. ? Rapid growth of broad-line food service distribution business. ? Diversification continues in formats and menus, including take-out, food court, fusion cuisine, foreign ethnic cuisine and wine.

* Notes:

1/ GNP: Gross National Production, Per Capita

2/ as of 2004

Source: Na, J.K., Understanding Food Service Industry (1998), Industry Sources

Below is a list of areas where major changes are currently taking place in the local restaurant segment:

- Reducing operation costs by using more part-time employees, adopting central kitchen facilities, standardization of recipes and product specifications, adopting information technology solutions such as POS (Point Of Sales) systems, ERP (Enterprise Resource Planning) systems and RFID (Radio Frequency Identification Tag) systems.
- Minimizing the amount of products in inventory by switching to broad-line suppliers and further processed products. Many franchise restaurant chains are switching to broad-line suppliers on a long-term contract for more efficient product purchasing. As a result, mergers and acquisitions of companies, both in restaurant operation and product distribution, are actively pursued.
- Diversification of menus with foreign ethnic cuisines and ingredients.
- Diversification of restaurant concepts and designs reflecting changes in the consumption and cultural trends. Natural, organic, fresh, fusion, Zen, fun, ethnic and neighborhood are some of the key themes in the market.
- There has been a greater emphasis on health and food safety by introducing more functional and organic ingredients, HACCP certification, and promotional activities under this theme. Sales of local restaurants are extremely sensitive to food safety issues and have experienced significant fluctuations in recent years from nation-wide food scares, including BSE, avian influenza and parasite eggs in Kimchi.
- There has been a greater emphasis on cross-promotional partnerships with non-food businesses, such as information technology, movie and finance. Sales promotions are heavily targeted to holidays and special occasions, including New Years' Day, Lunar New Years' Day, Valentine Day (Feb. 14), White Day (March 14), Kid's Day (May 5), Parent's Day (May 8), Teacher's Day (May 15), Korea Thanks-Giving Day and Christmas.

Table 6: Break Down of Restaurant Segment by Type of Restaurant (2001^{1*})

Type of Restaurant	# of Restaurants	Annual Sales	# of Employees
Full Svc Korean Restaurants	45.3%	43.1%	44.6%
Full Svc Chinese Restaurants	4.8%	4.5%	5.3%
Full Svc Japanese Restaurants	1.0%	2.8%	1.9%
Full Svc Western Restaurants	2.6%	4.9%	4.0%
Institutional Feeding Restaurants	0.5%	2.4%	1.7%
Quick Svc Western Restaurants	4.8%	7.9%	6.0%
Quick Svc Korean Restaurants	9.8%	5.4%	7.2%
Bars and Pubs	21.5%	19.6%	20.1%
Bakery Shops	1.7%	2.2%	1.8%
Tea & Coffee Shops	6.7%	4.6%	5.9%
Total	505,241	₩ 34,245,594 mil	1,341,528

* Note: 1/ Year 2001 is the most recent year for which data is available.

Source: Korean government statistics (Dec. 2004)

Although declining in number due to the rapid growth of international restaurants, traditional Korean food restaurants are still very popular. It is, however, becoming more difficult to distinguish Korean menus from foreign ones, as more diverse recipe ideas and food styles are introduced, fusing traditional menus with new-to-market recipes and ingredients. At the same time, foreign-oriented dishes served in restaurants in Korea are somewhat 'Koreanized' in terms of the taste, ingredients used, and cooking style. In particular, local consumers prefer less salt, fat and oil, while eating more hot spices, vegetables, seafood and soup.

Due to the high population density, delivery service is commonly offered by restaurants in metropolitan areas. For example, the Pizza Hut chain makes 70 percent of its sales from home delivery service. The high cost of real estate and space rent is also forcing small-scale restaurants focus on the home-delivery market.

It is notable that Korea has an exceptionally high number of bars and pubs. The newest trends in the segment include micro-brew pubs, wine bars and the growth of bars under franchise management. Although decreasing among the health-conscious elderly generation and young professionals, drinking is still considered a very important part of business and social life. According to government statistics, each Korean adult over the age of 19 consumed 26 liters of Soju (local hard liquor) and 53 liters of beer in 2003, up 5 percent and 81 percent respectively from ten years before. The rapid growth of wine and other low-alcohol beverages has come at the expense of hard liquors. Recently, the number of expensive drinking saloons and the consumption of premium whisky has significantly declined as a result of a new government regulation that excluded corporate spending in bars over certain limit from tax deduction.

Growth of fast food restaurants has stagnated in recent years due partly to the on-going economic slowdown and more largely to consumers' growing concerns about healthy eating. In particular, BSE and avian influenza scandals in recent years further deteriorated consumer confidence in beef and chicken meat, staple fast food products. As a result, several fast food chains, including Hardies, Wendy's and BHC(a local hamburger chain), went out of business and leading chains have seen closings of many 'slow moving' outlets. Lowering prices and introducing new, healthier menus are the two major counter measures being implemented in the industry. In spite of the challenges facing the industry, there has been a continuous flow of new restaurants added to the segment armed with new recipes and themes, reflecting the strong consumer demand for new tastes and quick services. A good example is the Papa Jones pizza chain, which has expanded considerably with 35 new store openings during the last two years. According to a Korean government survey in 2004, 135,000 consumers, which was 0.27 percent of the population, ate fast food at least once a day. Another survey in the same year showed that 2.6 percent of Korean children ate fast food at least once a day.

Table 7: Profile of Major Quick Service Western Restaurant Chains (2004)

Company	Brand	Annual Sales	# of Outlets	Change of # Outlets in 2004
Lotteria Co.	Lotteria	₩450 billion	839	-51
Shinmac / Mackim	McDonald's	₩300 billion	335	-8
Genesis	BBQ	₩450 billion	2,500	+950 ^{1*}
SRS Korea	KFC	₩170 billion	195	-13

	Burger King	₩76 billion	95	-13
TS Haemaro	Popeye's	₩100 billion	180	-30

* Note: 1/ Genesis's acquisition of BHC chain in 2004 caused the big increase.
Source: The Yearbook of Retail Industry 2005, KOSCA

Table 8: Profile of Major Family Restaurant Chains (2004)

Company	Brand	Annual Sales	# of Outlets	Change of # Outlets in 2004
Food Star	TGIF	₩100 billion	33	+8
Rise On	Bennigan's	₩83 billion.	20	+1
Amoje	Marché	₩30 billion	9	-1
CJ Foodville	VIPS, SkyLark	₩120 billion	76	-1
Ojjung	Outback Steak	₩160 billion	50	+17
Sunat Food	Tony Romas	₩18 billion	7	0
Barons International	Sizzler	₩18 billion	6	+1

Source: The Yearbook of Retail Industry 2005, KOSCA

Table 9: Profile of Major Pizza Restaurant Chains (2004)

Company	Brand	Annual Sales	# of Outlets	Change of # Outlets in 2004
Pizza Hut Korea	Pizza Hut	₩390 billion	320	+20
Mister Pizza Korea	Mister Pizza	₩150 billion	220	+35
DPK International	Domino's Pizza	₩150 billion	247	+29
PJI Korea	Papa Jones	₩5 billion	18	+13

Source: The Yearbook of Retail Industry 2005, KOSCA

Table 10: Profile of Major Coffee Shop Chains (2004)

Company	Brand	Annual Sales	# of Outlets	Change of # Outlets in 2004
Starbucks Korea	Starbucks	₩72 billion	109	+35
Rosebud	Rosebud	₩28 billion	267	+13
Coffeebean Korea	Coffeebean	₩31 billion	34	+9
SPC Group	Pascucci	₩13 billion	14	+3

Lotteria	Java Coffee	₩9 billion	21	+7
Barons International	Cafe Nescafe	₩4 billion	27	+2

Source: The Yearbook of Retail Industry 2005, KOSCA

3. Institutional Food Service Segment

Table 11: Profile of Major Institutional Food Service Companies (Year 2004)

Name of Company	Annual Sales	# of Outlets	Change of # Outlets in 2004	# of Serving Units Daily
Our Home	₩540 billion	600	+100	700,000
Samsung Everland	₩500 billion	480	+30	500,000
CJ Food System	₩205 billion	539	-90	400,000
Hyundai Food System	₩220 billion	380	+80	200,000
Shinsegae Food System	₩263 billion	360	+10	150,000
Arakor	₩90 billion	320	+50	250,000
ECMD	₩90 billion	280	+30	180,000
Hanwha Development	₩100 billion	210	+5	160,000

Source: Korea Food Distribution Yearbook 2005, Monthly Food Journal

Institutional food service restaurants are growing, as more office workers and students are seeking cheaper meal options. Institutional food service includes feeding service operations with exclusive contracts in schools, offices, manufacturing plants, hospitals, retirement homes and government facilities. In most cases, the client company/organization endows an exclusive, long-term contract for designated feeding services (mostly lunch and dinner for a designated group of people) to the institutional food service operator through a bidding process. Basically, it is the client who pays for the services on behalf of the group of people accessing the feeding service, although in some cases, the operator maintains a right to open the restaurant to outside customers for additional sales. A major trend in the market is switching to a commercial outside institutional feeding operator from the traditional in-house system (Korean companies have a tradition of providing free meals to employees). The annual cash register sales of the segment for 2004 was estimated at ₩5.8 trillion, about 50 percent of which was taken by commercial institutional food service operators. Another half of the market still relied on in-house restaurants operated and owned by the client organization. Commercial institutional food service providers are expected to further increase their market shares in the coming years, as more organizations seek cheaper and more efficient way to provide quality meals for their employees and students.

In general, the growth of the institutional feeding restaurant segment is mainly led by a handful of leading players, all of them subsidiary businesses of local conglomerates. Focusing on big volume clients for economy-of-scale, the leading players are closing down small-scale outlets, leaving behind some room for smaller competitors to enter and grow. Especially schools and hospitals are changing hands to smaller but dedicated operators.

Most of the leading institutional feeding companies have diversified into regular restaurant businesses, including food courts, cafeterias, bars, coffee shops, bakery shops and premium restaurants. In addition, leading companies have also entered the food service distribution businesses, partly in an effort to achieve greater buying power. However, products distributed by these institutional feeding companies are currently limited to those products that they themselves use in large volumes. It is expected that the distribution arms of these companies will someday evolve into separate, independent broad-line food service distribution companies, handling wider variety of products.

The cost of food products comprises about 60 percent of the total operation cost in an institutional food service company, which is much higher than that of a regular restaurant, which is about 30 percent. Consequently, companies in this segment are extremely conscious about the price, value and stable supply of products. Imported products mainly used in the segment, therefore, are mostly price-oriented products from China, South Asia and Australia. Leading companies are currently trying to incorporate more further-processed products in an effort to reduce labor and overhead cost.

Section III. Competition

Domestic products, both raw and processed, comprise a major competition to many U.S. products. Although limited in variety, Korean agriculture produces a considerable amount of raw agricultural products, including rice, fresh vegetables, fruits, seafood, pork meat, chicken meat, egg and fluid milk. In addition, Korea has a strong processed food industry that manufactures a wide variety of products, including processed meat, seafood, vegetables, fruits, noodles, sauces, oils, beverages, snacks, bakery, confectionaries, dairies and liquors. For raw agricultural products and input ingredients for the local processing industry not grown or manufactured in Korea, U.S. products face increasing competition from imported products from other countries. Products from competitor countries, including China, Australia, Chile and Thailand, in general have lower prices than U.S. products and, thus, are quickly building up market shares. China, for example, has become the biggest supplier of fresh and processed vegetables, sauces, spices, seafood and grains to the Korean food service sector. In addition, increased demand for more diverse international cuisines and recipes are translated into growing demand for imported products from more diverse origins, including European and South Asian countries.

Lifting of import barriers directly affects competition in the market. Many local products have lost price and availability competitiveness when protective import barriers were removed, which is expected to happen continuously in the coming years. Since the implementation of the Korea-Chile Free Trade Agreement (FTA) in April 2004, trade between the two countries has reached record levels. Korea has also concluded two other FTAs with Singapore and FFTA (agricultural products were not included) and has readily engaged in FTA talks with several other countries in 2005. The United States and Korea announced in February 2006 that they would begin FTA discussions, which are expected to conclude in mid-2007.

As tariff barriers decline, food safety issues are becoming more a means for the Korean government to restrict imports. Restriction of imports from certain countries results in replacement imports from competing countries, as seen in the import ban on U.S. beef for BSE. Consequently, in an effort to maintain a stable supply, food service distributors in general prefer to transact with more than two different countries especially for potentially risky items, such as chicken meat, pork meat and beef.

IV. Best Product Prospects for U.S. Exporters

A. Products Present in the Market Which Have Good Sales Potential

1. Pork meat (chilled and frozen belly cut): Due to the import ban on U.S. beef since December 2003, many beef restaurants have switched to pork menus, resulting in a strong demand for additional imports. Although Korea has a large domestic supply of pork meat, local demand is highly skewed to the belly cut, which has resulted in a strong need for imports. It is interesting to note that much of the meat is distributed frozen in the food service sector, as restaurants generally want longer shelf life. During 2005 through November, total pork meat imports increased 79 percent from the previous year, to \$537 million. Imports from the United States during that same time period also showed an explosive growth of 269 percent to \$120 million.

2. Processed meats (sausages, hams): Due to easy application, a wide variety of local menus incorporate processed meat products. Fast food, bars and buffet restaurants are the main users of these products. Imports of sausages grew 39 percent in 2005 through November to \$9.8 million (most of them from U.S.) while imports of preserved meat grew 118 percent to \$42 million (\$2.9 million from U.S.).

3. Chicken meat (frozen and processed): Although there still remains some safety concerns among consumers over poultry products due to the on-going Avian Influenza issue, Korea remains an excellent market for chicken meat products. In particular, the import ban on U.S. uncooked poultry products was lifted in 2005, resulting in a 588 percent increase of imports from the United States through November to \$30 million, accounting for 37.6 percent of total poultry product imports. Demand for further processed poultry products is expected to grow gradually in the future, as more restaurants understand the cost savings of value-added products. Conversely, Korean food service sector is not a market for imported fresh chicken meat due to the short shelf life and strict sanitary standards (zero tolerance on E-coli contamination) on imported fresh meat.

4. Seafood (frozen and processed): Korea is an outstanding seafood market with good growth potential for imported products. The domestic supply is decreasing due to the depletion of near sea fishery resources and increased international restrictions on deep-sea fishing. Total imports of fishery products amounted to \$2.1 billion in 2005 (through November), up 3.5 percent from the previous year, while imports from the United States grew 10.5 percent to \$130 million. Major species currently imported from the United States include: Alaska Pollack, Pollack surimi, Pollack roes, tuna, skate, mackerel, hagfish, halibut, scallop, cod, Pacific salmon, angler fish, rock fish, and prepared sea cucumber. It is notable that demand for processed products (fillet, dried, surimi, and cooked) are also rising. Processed products (fillet, dried and salted) accounted for about 24 percent of total seafood imports in 2005.

5. Processed fruits and nuts: Processed fruits and nuts are gaining consumer popularity for their natural and healthy image. Introduction of new recipes that require processed fruit and nut ingredients is resulting in growing demand for more diverse products. Imports of processed fruits and nuts from the United States amounted to \$16 million in 2005 through November. Products currently imported from the United States include: dried, frozen, or preserved prunes, cranberries, cherries, strawberries, grapes, figs, blueberries, walnuts, almonds, pistachios, pecans and peanuts. Fruit juices also have a big market in Korea, as U.S. products, at \$33 million imports in 2005, took a 35 percent import market share.

6. Fresh fruits: Korea is an excellent market for U.S. oranges. Demand for imported oranges is increasing in both food service and retail sectors. Currently, U.S., Australia and South

Africa are allowed to export oranges to Korea. Orange imports from the United States in 2005 through November amounted to \$116 million. Other U.S. fruits currently imported into Korea include table grapes (\$7 million), lemons, cherries (\$7 million) and grapefruits.

7. Vegetables (fresh, frozen, canned and prepared): Although Korea is self-sufficient in many varieties of fresh vegetables, seasonal fluctuations in the local supply and unfavorable growing condition for foreign varieties are resulting in an increased demand for imports. China has emerged as the leading supplier of vegetables to the Korean food service sector in both the fresh and processed category; however, there remains a solid demand for a limited variety of high-quality U.S. products. Major products imported from the United States include potatoes, onions, lettuce, tomatoes, broccoli, avocados and carrots. Imports of vegetables from the United States amounted to \$21 million in 2005 through November, with an additional \$49 million of imports of prepared vegetable products.

8. Dairy Products (milk concentrate, cream, whey, butter and cheese): Diverse recipes with dairy ingredients are steadily being introduced, resulting in a growing demand. In addition, there is an increased demand for imported dairy products from the thriving bakery industry. Imports of milk concentrate and cream grew 80 percent in 2005 (through November) to \$17 million (unfortunately, only \$192,000 came from the United States). Imports of whey grew 25 percent to \$80 million, while U.S. products grew 105 percent to \$21 million. Imports of butter grew 49 percent to \$12 million (only \$65,000 from U.S.). Imports of cheese amounted to \$128 million, up 19 percent from the previous year, while imports from the United States also grew 28 percent to \$23 million.

9. Alcohol Beverages (wine, beer and hard liquors): With the large number of bars and pubs, imported alcohol beverages maintain a sizable market in the food service sector. Especially demand for products with health benefits and lower alcohol content is rapidly growing. Wine imports increased 16 percent in 2005 through November to \$60 million, setting a record-high. Imports from the United States also set a new high at \$8.5 million, up 15 percent. Among the \$15 million of beers imported in 2005, U.S. products, at \$4 million, took 27 percent of the market. Imports of U.S. hard liquor products totaled \$3.3 million in 2005, which constituted only 1.4 percent of total hard liquor imports.

10. Coffee: On-going expansion of franchise coffee shop chains results in an increased demand for imported coffee. Imports of coffee from the United States grew 27 percent during 2005 through November to \$5.7 million.

11. Sauces and Condiments: With introduction of more diverse foreign recipes, demand for imported sauces and condiments is rising. Imports from the United States in 2005 through November grew 18 percent from the previous year to \$13.4 million.

B. Products Not Present in Significant Quantities But Which Have Good Sales Potential

1. Deboned beef meat: Korean government lifted import ban on deboned beef meat from the United States in January 2006. The new regulation states that only beef meat, free of any bone or SRM, from cattle under 30 months old from pre-approved slaughter houses/packing plants in the U.S. are allowed.

2. Rice: The new rice trade agreement that Korea signed with exporting countries will allow imported rice to be distributed commercially through retail channel starting in early half of 2006. It is expected that some portion of the imported rice, including U.S. rice, will be used by the food service sector. Imported rice will gain more price competitiveness over the

coming years, as the agreement is made to gradually increase the volume of imported rice with access to the commercial retail market.

3. Pasta: Increased popularity of Italian recipes is resulting in a rapid import increase of products related to the cuisine, including Pasta. Unfortunately, among the \$50 million of pasta products imported in 2005 through November, imports from the United States amounted to a mere \$500,000.

4. Ingredients for Mexican cuisine: Many industry experts predict that Mexican cuisine has a great potential in Korea, as the cuisine contains a lot of hot, spicy dishes. However, unfortunately, there are very few chefs and restaurants in the market where good Mexican food can be found.

5. Processed turkey meat: Somehow, local mainstream consumers still maintain a negative view on turkey meat. However, with millions of Koreans traveling to the United States every year, processed turkey meat products continue to gain some support, especially from young consumers. Turkey ham sandwiches are already getting popular among affluent, young consumers.

6. Premium seafood: Products such as lobster, crabs (King, Snow, and Dungeness), black cod and wild-caught Sockeye salmon have good potential in Korea as affluent consumers are looking for new, premium and healthier alternatives to beef and pork. These premium products also have a good potential as gift items.

7. Processed eggs (fluid, frozen and flour): More restaurants and bakery shops are expected to switch to processed egg products from shelled eggs.

8. Prepared processed food: Demand for prepared products, such as frozen soups and fully cooked meals, is gradually picking up in the food service sector. As more restaurants understand the economic benefit and quality of prepared products, interest in U.S. products is likely to increase.

9. Ingredients for micro-brew beer: Demand for ingredients for micro-brew beer is likely to increase with the addition of more micro-brewery restaurants, which are gaining in popularity.

10. Processed Organic products: The demand for processed organic products continues to increase due to the strong interest of affluent consumer groups and young mothers.

11. Many imported agricultural products, including honey, fresh potatoes, fresh onions and popcorn, are subject to high tariffs and tariff rate quotas (TRQs) that restrict import volumes. However, on-going trade negotiations are likely to reduce some of these barriers in the coming years.

C. Products Not Present Because They Face Significant Barriers

1. Beef meat from cattle over 30 months old, bone-in beef meat, processed beef products and offal: Before the import ban, annual export of U.S. beef products to Korea amounted to around \$900 million. Although the ban is now lifted on boneless beef meat from cattle under 30 months old, the ban remains to meat from cattle over 30 months old, bone-in meat, processed beef products and offal.

2. Lamb meat: Imports of U.S. lamb meat is banned, as imports of products of all ruminant animals, except boneless beef, are currently banned due to the BSE issue.

3. Imports of many U.S. fresh fruits, including apples, fresh berries, pomegranates and mangos, are prohibited as there is no bilateral plant sanitary quarantine agreement between the U.S. and Korea.

4. Fresh organic produce: imports of fresh organic produce are unlikely in the near future due to the lack of organic certification equivalency.

V. Key FAS/USDA Contacts and Further Information

? For further information about the Korean agricultural market, please contact:

U.S. Agricultural Trade Office

Korean Address: Room 303, Leema Building, 146-1, Susong-dong, Chongro-ku, Seoul 110-140, Korea

U.S. Mailing Address: U.S. Embassy Seoul, Unit 15550-ATO, APO, AP 96205-5550

Telephone: 82-2 397-4188

Fax: 82-2 720-7921

E-mail: atoseoul@usda.gov

Website: www.atoseoul.com

Agricultural Affairs Office

Korean Address: U.S. Embassy, 82, Sejong-ro, Chongro-ku, Seoul, Korea

U.S. Mailing Address: US Embassy Seoul, Unit 15550-AgAff, APO, AP 96205-5550

Telephone: 82-2 397-4297

Fax: 82-2 738-7147

E-mail: agseoul@usda.gov

? For further information about sanitary and phytosanitary requirements, please contact:

U.S. Animal Plant and Health Inspection Service (APHIS)

Korean Address: Room 303, Leema Building, 146-1, Susong-dong, Chongro-ku, Seoul, Korea

U.S. Mailing Address: US Embassy Seoul, Unit 15550-APHIS, APO, AP 96205-5550

Telephone: 82-2 725-5495

Fax: 82-2 725-5496

E-mail: aphis@kornet.net

Website: www.aphis.usda.gov

? For information about activities by State Regional Trading Groups, please contact:

Mid-America International Agri-Trade Council (MIATCO)

400 West Erie Street, Suite 100, Chicago, IL 60610

Telephone: 312-944-3030

Fax: 312 944-1144

E-mail: eriggs@miatoco.org

Website: www.miatco.org

Western United States Agricultural Trade Association (WUSATA)

2500 Main Street, Suite 110, Vancouver, WA 98660-2697

Telephone: 360-693-3373

Fax: 360-693-3464

E-mail: bruce@wusata.org

Website: www.wusata.org

Food Export USA - Northeast Region of the United States

150 S. Independence Mall West, 1036 Public Ledger Building, Philadelphia, PA 19106

Telephone: 215-829-9111

Fax: 215-829-9777

E-mail: jcanono@foodexportusa.org

Website: www.foodexportusa.org

Southern United States Agricultural Trade Association (SUSTA)

E-mail: jim@susta.org

Website: www.susta.org

? For information on the commercial and industrial products in Korea, which includes farm machinery, cosmetic and pharmaceuticals, please contact:

U.S. Commercial Service

Korean Address: U.S. Embassy, 82, Sejong-ro, Chongro-ku, Seoul, Korea

U.S. Mailing Address: US Embassy Seoul, Unit 15550-USCS, APO, AP 96205-5550

Telephone: 82-2 397-4535 Fax: 82-2 739-1628

E-mail: Seoul.office.box@mail.doc.gov Homepage: www.buyusa.gov/korea