



USDA Foreign Agricultural Service

GAIN Report

Global Agriculture Information Network

Template Version 2.09

Required Report - Public distribution

Date: 6/18/2008

GAIN Report Number: CH8609

China, Peoples Republic of

Food Processing Ingredients Sector

Food Processing

2008

Approved by:

Joani Dong, Director
U.S. Agricultural Trade Office Guangzhou

Prepared by:

Evid Liu, Susan Zhang, Angie Han

Report Highlights:

China's food industry continues to grow rapidly. In 2006, some 26,000 food enterprises earning more than US\$ 625,000 annual gross industrial sales increased 27.3 percent from the previous year to US\$ 265.3 billion. Affluent coastal regions remain food processing centers while less developed regions have quickly developed their food processing sectors. High prices and food safety are key concerns for both industry and consumers. Despite substantial domestic production of many agricultural and food ingredients, China offers ample opportunities to the US, especially for soybeans, seafood, poultry products and meat, dried fruit and nuts, dairy ingredients, potato products, baking ingredients and food additives. Competition stems from both domestic producers and foreign competitors. Understanding the market and cultivating a reliable relationship with Chinese partners are crucial for U.S. exporters to succeed.

Includes PSD Changes: No
Includes Trade Matrix: No
Annual Report
Guangzhou ATO [CH3]
[CH]

Table of Contents

Table of Contents	2
Executive Summary	4
I. Market Review	5
1.1 Food Industry in China	5
1.2 Sector Size and Growth	6
1.3 Prices and Food Safety - Key Concerns for Food Industry	8
1.3.1 Prices	8
1.3.2 Food Safety	9
1.4 Kosher Certification in China	11
1.5 Regional Development of Food Industry	11
1.5.1 South China	11
1.5.2 East China	13
1.5.3 North China	14
1.6 Analysis of Product Categories	15
1.6.1 Oils and Fats	15
1.6.2 Dairy Products	16
1.6.3 Meat	18
1.6.4 Bakery	18
1.6.5 Baby Food	19
1.6.6 Beverage	20
1.6.7 Dried Fruit and Nuts	21
1.6.8 Confectionary	22
1.6.9 Seafood	23
1.6.10 Ice Cream	24
1.6.11 Quick Frozen Products	24
1.7 Market Opportunities and Challenges	26
1.8 Outlook for the Food Processing Industry in China	27
II. Roadmap for Market Entry	29
2.1 Entry Strategy	29
2.2 Distribution	29
2.2.1 Distribution pattern	29
2.2.2 Cold Chain	30
2.2.3 Potential of Air Freight	31
2.3 Company Profile	31
2.4 Sector Trends	34
III. Market Competition	35
3.1 Domestic Competition	35
3.2 Competition of Imports - 2007	38
3.2.1 Soybeans (HS Code: 1201)	38
3.2.2 Fish and Seafood (HS Code: 03)	39
3.2.3 Meat (HS Code: 02)	40
3.2.4 Edible Fruit and Nuts (HS Code: 08)	41
3.2.5 Dairy Products (HS Code: 04)	42
3.2.6 Preserved Food (HS Code: 20)	43
3.2.7 Cereal (HS Code: 10)	44
3.2.8 Fats and Oils (HS Code: 15)	45
3.2.9 Vegetables (HS Code: 07)	46
3.2.10 Preparations of Flour (HS Code: 1901)	47
IV. Best Product Prospects	48
V. Further Reference	48

VI. Post Contact Information.....	49
Appendix 1. Distribution Channel Members	50
Appendix 2. Import Documentation	51
Appendix 3. Good Prospects for Ingredients in China	52

Executive Summary

This annual report examines the China market for food processing ingredients in CY 2007. It reviews the country's food industry and sectors as well as regional development; analyzes various product categories, opportunities and challenges for U.S. exports in this market; and discusses the entry road map and related distribution issues. The report also explores competition from both domestic and imported food ingredients and recommends best product prospects.

The strong economy in China spur fast growth in the food processing industry, especially in grain and oil processing, meat processing, and dairy product manufacturing which had over 20 percent annual increases. Latest available statistics show that the country in CY 2006 had 26,326 food enterprises whose annual sales exceeded US\$ 625,000, and that the total annual sales by these companies rose 27.3 percent to US\$ 265.3 billion. Affluent coastal regions have long been the food processing centers in the country while less developed regions, such as Fujian, Guangxi, Henan and Inner Mongolia have quickly developed industrial food processing sectors. Surging prices and food safety were key concerns for both industry and consumers.

Fast urbanization, increasing disposable income and expenditure on food, changing life style and diet shape the industry's development in this fragmented market. Food consumption varies from region to region, making the country a cluster of many regional markets rather than a single market. Some sectors, including bakery, dairy products and baby food, grow faster than average due to fast paced lifestyles, more protein in the diet and improved quality-of-life. Large wealthy cities lead consumption trends.

The fast growing market in China provides ample opportunities but also challenges to U.S. ingredients suppliers. China as a large producer of many food and agricultural products, imports a large volume of various food as ingredients to meet the domestic demand. The US is a large supplier for China of high quality soybeans, poultry and meat products, seafood, fruit and nuts, dairy ingredients, grains and prepared or processed ingredients. Best product prospects for US exporters are soybeans, seafood, poultry products and meat, dried fruit and nuts, dairy ingredients, potato products, baking ingredients and food additives. Competition stems from both domestic producers and foreign competitors. For U.S. exporters to succeed, they must understand the market and engage in a reliable relationship with Chinese partners.

I. Market Review

1.1 Food Industry in China

China's strong economy boosts the food processing industry. Latest official statistics¹ show that in CY 2006, total industrial output by food enterprises above the designated size² grew 24 percent from the previous year to US\$ 265.3 billion (RMB 2,158.7 billion). Primary food processing, food manufacturing with more value added, and beverage manufacturing all have trended upwards in recent years (Table 1.1) . Steady growth is foreseeable, given the growing economy and increasing disposable income by growing middle and upper class of consumers.

About 60 percent of the industry's output comes from primary processing with limited value added, though the share of food and beverage manufacturing which generates higher value grows. Grain and oil processing, meat processing and dairy product manufacturing are top earners with over 20 percent annual increases.

Table 1.1 Above Designated Size Food Enterprises in China*

	2003		2004		2005		2006	
	Number	**Sales	Number	**Sales	Number	***Sales	Number	****Sales
Food Processors	11,192	70,495.5	12,244	94,108.1	14,575	126,420.6	16,356	158,684.6
Food Manufacturers	4,636	26,124.8	4,950	32,397.1	5,553	44,704.3	6,056	57,524.0
Beverage Manufacturers	3,194	25,508.8	3,332	29,332.7	3,519	37,259.5	3,914	49,059.4
Total	19,022	122,129.2	20,526	155,837.8	23,647	208,384.4	26,326	265,268.0
YY Growth %	3.9	23.4	7.9	27.6	15.2	33.7	11.3	27.3

* The table only includes those enterprises that realized annual sales over RMB 5 million in the reported years

** in 1,000,000 US\$. 1 USD = 8.3 RMB

*** in 1,000,000 US\$, 1 USD = 8.2 RMB

****in 1,000,000 US\$, 1 USD = 8.0 RMB

Data sources: China Statistical Year Books 2003 -2007

While coastal affluent regions surrounding Guangzhou, Shanghai and Beijing have long been the food processing centers in the country, while less developed regions, such as Fujian, Guangxi, Henan and Inner Mongolia, have quickly developed industrial food processing sectors in the past few years.

The food industry in China is fragmented, and consists of mostly small enterprises. Among the 448,000 food processors and manufacturers in the country, only 26,000 companies exceeded annual sales over US\$ 625,000 (RMB 5 million), collectively holding over 70 percent share of the market³. This group of larger-sized companies enjoys higher levels of productivity and profitability due to advanced management, facilities and market share.

¹ China Statistical Yearbook 2007

² Those enterprises with annual gross industrial output from primary business over RMB 5 million, or US\$ 625,000

³ The Status Quo of China's Food Quality and Safety by the State Council, 2007

Due to its large population, China as the second largest economy in the world, feeds the largest food consumer group in the world. The largest consumption in terms of volume includes edible oils and fats, alcohol and spirits, aquatic products, grains, non-alcohol beverage, meat products, dairy products and condiments. In addition to its substantial domestic production, China has to import various types of food in large volumes to meet domestic demand. Food expenditure accounts for a significant portion of household income, about one-third an average urban family and almost half a rural one.

China is a sizable exporter of aquatic products, vegetables, canned food, juice, grain and cereal products, condiments and poultry products to Japan, US, EU and South East Asian countries, mainly due to inexpensive labor cost.

Only 30 percent of food in China is processed, compared to about 60-80 percent in western countries. While most consumers still prefer to buy fresh foods, the market for processed foods is growing, especially in urban areas where higher concentrations of wealth and busier lifestyles have led many to look for more convenient alternatives.

Food quality and safety have drawn unprecedented concerns in the past year. Enormous media exposure of substandard food products and excessive residues, consumers' loss of confidence, as well as condemnation from foreign countries created a crisis of confidence for "Made-in-China" products. To save the country's reputation and reinstate consumer confidence, the central and local governments executed a series of "rectifying campaigns" to govern the food industry. Consequently, consumers have gained increasing awareness of food quality and safety, which spells opportunities for high quality food products.



*International food ingredients companies exhibited at Food Ingredients China 2008 trade show.
(Source: ATO Guangzhou)*

Demands for healthy choices, convenience, well-being and growing preference among the younger population towards western styles of food open the door to high quality imported ingredients. Recent food poisoning incidents have also awakened consumer concern over food quality and safety, and many now look towards food products that are packaged with big-name brands they feel they can trust. In many urban areas, 40 percent of food is processed which shows promising growth. Furthermore, China's inexpensive labor makes it a profitable center for export-oriented production.

Globally surging food and fuel prices significantly impact the food industry. Almost all food products, including cooking oil, rice, baked goods and ice cream, are retailed at much higher prices than a year ago. Record breaking fuel prices have increased the cost of transport and manufacturing. Despite the strong Chinese currency, the price surge prohibits imports of many commodities including soybean, wheat and whey from the US.

1.2 Sector Size and Growth

The food industry in China is comprised of a large number of companies from very small family run workshops to global corporations. Most companies are small scale, characterizing the very fragmented nature of the industry. In 2006, China had in total 446,000 food enterprises, among which only 26,000 or 5.8 percent of the total food enterprises, exceeded

a designated level of annual sales of US\$ 625,000 (RMB 5 million). However, this group of larger size companies accounted for 72 percent of the market share (Table 1.2), especially in the rural and less developed regions. Overall, the group of large size enterprises outperforms the small size companies, due to the economies of scale, better product quality, and advanced operation and management.

Chinese official statistics categorize industrial food production as:

- food processing, including primary activities such as rice milling, flour milling, oil refining, sugar refining, slaughtering, salt processing, feed processing, and aquatic product processing;
- food manufacturing, consisting of packaged food, pastries and confections, dairy products, canned foods, fermented products, and condiments;
- and beverage manufacturing, as in production of alcoholic beverages (i.e., distilled spirits, beer and wine), soft drinks and tea.

Table 1.2 Food Industry in China

	Number of enterprises	% of total enterprises	Market share (%)
Above designated size*	26,000	5.8	72.0
Under designated size of more than 10 employees	69,000	15.4	18.7
Fewer than 10 employees	353,000	78.8	9.3
Total	448,000	100.0	100.0

*Designated size: annual sales of US\$ 625,000 (RMB 5 million)

Data source: *Status Quo of China's Food Quality and Safety White Paper*, State Council of China, 2007

All these categories have had steady growth, thanks to increasing expenditure on food and urbanization. In 2006¹, the group of the above designated sized companies in the industry recorded sales growth of 25.5 percent in primary food processing, 28.7 percent in food manufacturing and 31.7 percent on beverage manufacturing. Primary processing of food, accounting for almost 60 percent of sales revenue, is the largest contributor to the industry while food and beverage manufacturing, which have more sophisticated operations and generate higher value, gradually increase respective share in the industry. Such change in the composition is mostly driven by more consumers who are developing more sophisticated demands in terms of food quality, product varieties, convenience, nutrition and well being.

¹ Latest full year available data. The data include only those companies with annual sales of US\$ 625,000 (RMB 5 million) or more. Data source from *China Statistical Yearbook 2007*.

1.3 Prices and Food Safety - Key Concerns for Food Industry

1.3.1 Prices

Price surges of many commodities have become a hot topic in the Chinese food processing industry. Record-breaking increases on crude oil prices have placed pressure on transportation and energy costs, and worse still are the skyrocketing prices of commodities including soybean, corn and wheat due to global short supply and strong demand which has beefed up prices of many raw materials for food processing and manufacturing. Pork, oilseeds, wheat, and dairy products saw the greatest price increases this past year. Global surging prices have limited China's imports of food commodities.

Price fluctuations have greatly impacted trade. Take a look at the following:

Wheat

Since 2006, globally high wheat prices resulted from greater demand plus short supply, rising fuel and freight prices have prevented Chinese millers from using imported wheat to make high quality flour. China Customs' statistics show that in CY 2007, China's wheat imports (mostly *Durum* from Canada and Australia, and, *Hard Red Winter*, *Hard Red Spring* and *Dark Northern Spring* from the US) dropped over 85 percent in volume terms to only 83,424 MT from the previous year. Despite domestic flour price increases, the milling industry's profit margins have been squeezed as wheat prices far outpaces price increases for flour. Out of cost concerns, millers are shifting from imported wheat to domestic Chinese wheat of which the quality has been gradually improved. To secure the supply to domestic demand and lower increasing food prices, the central government has withdrawn the tax rebate on Chinese exported wheat products (regardless of origin), and instead, implemented a 20-25 percent tax on Chinese exports of wheat and wheat flour products effective January 2008.

Tree Nuts

In 2007, dropping prices due to high production and depreciating U.S. dollar dramatically boosted China's imports of nuts from the US, including pistachios (mostly *Kerman*), almonds (mostly *Carmel* and *Nonpareil*), walnuts, hazelnuts (mostly *Barcelona* and *Ennis*) and pecans (mostly *Western Schley* and *Stuard*). Statistics from *China Customs* showed that in CY 2007, imports of U.S. pistachios reached 8,728 metric tons, 80 percent up from the previous year. Imports of in-shell almond rose 43 percent to 935 tons, shelled almond up 47 percent to 965 tons, in-shell walnuts up 97 percent to 1,991 tons and in-shell hazelnuts up 1.4 times to 1,156 tons.

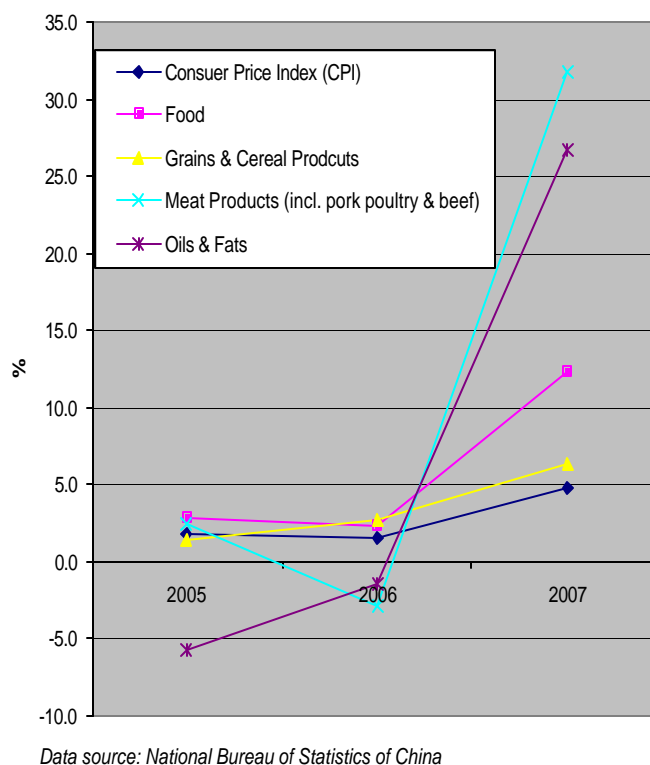
Dairy Products

In recent years, prices for dairy products have fluctuated, and there have been other factors that affected trading from and into China. Despite low domestic milk production, high prices in overseas markets drove China's dairy exports in CY 2007 to record high levels - 135,000 tons (mostly milk and powdered milk) in volume terms, a 80 percent leap. However, import volumes (mostly whey and powder milk) dramatically dropped, 9 percent on whey imports to 168,000 tons, and 27 percent on powdered milk to 99,000 tons. EU's dairy production quota and elimination of subsidies on dairy exports together with the weakening U.S. dollar have made U.S. products more price competitive in this market. Short supply from Australia due to the drought in past years has also cultivated increasing interest in sourcing U.S. dairy ingredients.

As a result of surging commodity prices, retail prices of food recorded significant increases. China's National Bureau of Statistics recorded a 4.8 percent increase on Consumer Price Index (CPI) in 2007, tripling the 1.5 percent increase in the previous year. Food prices rose at a much faster pace, overall a 12.3 percent increase from the previous year. Meat products (including pork, poultry and beef), oils and fats, as well as eggs increased the most, respectively 31.7, 26.7 and 22.9 percents up from CY 2006 (Figure 1). Prices for pork, for example, even had a much steeper surge. Despite the government's many control measures to ease inflation, the CPI still recorded a 8 percent increase in the first quarter of 2008.

Due to fluctuating prices, imports might be overvalued by customs and therefore subject to overly high import duties and Value Added Tax (VAT), and, in turn, restrict imports through official channels. In such case, it is crucial to present customs with solid convincing documentation, e.g., market price information, contracts, invoices, Bill of Lading (B/L), and payment evidence for revaluation. (Refer to GAIN Report CH 8025 for more information on prices in China.)

Figure 1. Price Increases in China



1.3.2 Food Safety

Tremendous media exposure of chronic food safety problems in China in the last few years stimulated a great deal of concern from the government, the industry and consumers. To prevent reoccurrence, the central and regional governments imposed substantial measures, from legislation to regulation enforcement, to rectify the industry. The central government also decided to strengthen and streamline inter-agency coordination and create a more effective food safety monitoring system. Last August, the country launched an ongoing nationwide product safety inspection campaign to reinforce inspection and safety enforcement in food processing, manufacturing and distribution. In addition, the national government actively fosters global cooperation to improve and ensure food safety.

Food Safety Administration

Food safety monitoring in China involves a number of governmental agencies at both the national and local level, including the *Ministry of Health* (MOH), the *Ministry of Agriculture* (MOA), the *General Administration of Quality Supervision, Inspection and Quarantine* (AQSIQ) as well as several other ministries and government agencies. No single agency is responsible for all food safety regulations and enforcement, and the distinctions between

different responsibilities (lawmaking, supervision, and enforcement) can be confusing. The basic difference between organizations as they relate to imported agricultural products is the following:

- MOH sets standards on food and products having to do with food and ingredients. For example it sets maximum residue levels MRL's for food additives, processing aids, contaminants, and pathogens (with the exception of pesticides which is done by MOA). This year the former *Chinese State Food and Drug Administration* (SFDA) disbanded and its overall food safety coordination role was returned to MOH.
- MOA sets standards for primary agricultural inputs and outputs. For example, they regulate animal feed, products of biotechnology (such as seed or yeast), and agricultural chemicals (including herbicides and pesticides). Critical MOA functions include the registration of new animal feeds and issuance of biosafety certificates for products containing biotech contents. Products can be regulated by either MOA or MOH depending on the level of processing or its stage of production. Deproteinized whey, for example, used as food is subject to MOH standards while its feed grade equivalent is subject to MOA regulation and standards.
- AQSIQ is strictly empowered to make sure that imported products conform to Chinese or equivalent standards and that imports meet the conditions of any bilateral trade protocols, which it generally negotiates with input from the Chinese domestic regulatory agencies. Thus, CIQ inspectors are tasked with protecting the animal, plant, and human health and safety of China.

The State Council approved the first draft of the Food Safety Law of P.R. China in October 2007 and the final draft is currently open for public comment. Once effective, the new law will replace the current Food Hygiene Law issued in 1995. The new law's basic aim is to clarify regulatory responsibility and place rule-making squarely on a scientific basis. In other words, the law is an attempt to increase the use of a risk based approach in the development of food safety standards for domestic products and imports. It addresses regulation, surveillance and enforcement throughout the production and marketing chain. In particular, the law will focus on food processing, distribution and sales.

Tightened Inspection on Imports

The Entry and Exit Inspection and Quarantine Bureaus of China (CIQs) at ports of entry - AQSIQ's regional subsidiaries - have redoubled efforts to check documentation of imported foods (including food ingredients), food additives, containers and packing materials. An import permit, for example, is required for some commodities, though not consistently. Thus, when asked, regular importers who did not hold such a document had shipments retained. To eliminate such inconveniences, exporters should keep close contact with the Chinese partner (importers, import agencies and declaration agencies) to have a clear understanding of import requirements as well as the up-to-date *de facto* practice.

Food importers have seen increasing hold-ups of cargo and slow shipment clearance at the ports of entry across the country due to tightening inspection. AQSIQ publicized 168 cases for January 2007 of imported food and cosmetics that failed to meet China's import requirement. The number of cases in question for March of the same year rose to 358, and to 436 in May. Shipment clearance takes much longer than before. In Guangdong, for

instance, it used to take only one day for the shipment to pass inspection and customs clearances at the port of entry. Since tightened scrutiny, it takes four or five working days to clear cargo, a significant lag.

Lag in Current Standards

Some existing Chinese standards run against the practice of food processing in developed countries, hampering imports of certain products. Take frozen concentrated grape juice as an example. China's national Hygienic Standard of Concentrated Fruit and Vegetable Juice for Food Industry (GB 17325 – 2005) sets the minimum acceptance level for yeast in juice of less than 20 colony forming units per milliliter (cfu/ml). Concentrated grape juice making in many major producing countries where the cold chain system is well-established employs a freezing process that keeps the juice as fresh as possible. It is difficult for concentrated grape juice made using the freezing process to meet the limit set in the current standard, as the process does not involve heat treatment to kill microorganisms. A similar conflict also exists for other products, such as sulfur dioxide in golden raisins or protein content for deproteinized whey for food usage. Such standards are likely to amount to a trade barrier that prevents related products from entering the China market.

1.4 Kosher Certification in China

The Chinese food industry is beginning to obtain kosher certification. Key kosher certificates, including *Circle U*, *Circle K* and *Star-K*, have limited presence in the industry, and there is almost no awareness of kosher certificates among Chinese consumers. Food or ingredients producers in China are certified because its major overseas clients require it. A constraint for kosher certification in China is limited awareness and understanding of kosher certification. Despite the large number of food enterprises in China, only 300+ companies have the *Circle U* kosher certification and 100+ for the *Circle K* certification. Most certified companies produce fruit and vegetable based products. No meat and dairy products are certified in the country due to difficulties to audit raw input. Since kosher certification in the US is a given with most major brand products, Chinese producers have to follow suit. Such certification adds product value and expands the customer base to include those that believe it further ensures a safe and healthy product.

1.5 Regional Development of Food Industry

China's food processing industry is intensively located in the most developed affluent regions along the coast, including Guangdong, Shanghai, Jiangsu, Zhejiang, Shandong, Beijing and surrounding areas. Some less developed provinces, such as Fujian, Guangxi, Henan, Inner Mongolia, as well as Liaoning, have quickly developed commercial food processing industry of large operations, taking advantage of easy access to large volumes of locally produced raw materials and low land and labor costs.

1.5.1 South China

South China, particularly Guangdong province, as the most industrial and urbanized region in the country, houses numerous well-established food companies. The food industry there enjoys a high reputation nationally for its good product quality, high productivity and innovation on technology and products.

South China processes a large volume of rice, wheat flour and other staple, cooking oils, beverage, poultry, seafood, dairy products, baked goods, dried and preserved fruit, nuts and confectionaries to serve both the domestic and export market. (See Table 1.3 for details of food enterprises in the region.)

Table 1.3 Food Processing Industry in South China by Province 2006*

		Number of Enterprises	Annual Sales** (million US\$)
Guangdong	Food Processors	761	10,521.4
	Food Manufacturers	627	5,934.0
	Beverage Manufacturers	203	4,491.5
	Total	1,591	20,946.9
Fujian	Food Processors	N/A	5,586.9
	Food Manufacturers	N/A	2,533.3
	Beverage Manufacturers	N/A	1,595.8
	Total	N/A	9,715.9
Hunan	Food Processors	589	4,311.0
	Food Manufacturers	237	2,070.3
	Beverage Manufacturers	152	875.5
	Total	978	7,256.8
Guangxi	Food Processors	354	5,784.5
	Food Manufacturers	113	434.9
	Beverage Manufacturers	96	789.9
	Total	563	7,009.3
Hainan	Food Processors	127	933.0
	Food Manufacturers	37	348.0
	Beverage Manufacturers	35	399.4
	Total	199	1,680.3
Regional Total * * *		3,331	46,609.2

* latest available data, including only those enterprises that realized annual sales over US\$ 625,000 (RMB 5 million) in CY2006

** US\$ 1 = RMB 8.0

*** Regional total of enterprises number exclude Fujian province due to available data

Data sources: *Statistical Year Books 2007* of reported provinces and cities

Geographically, food processing operations in South China heavily center in Guangdong, especially in the Pearl River Delta area covering Guangzhou, Shenzhen, Dongguan, Foshan, Zhongshan, Jiangmen and Zhuhai. In addition, Shantou and Chaozhou in Guangdong, and Jinjiang in Fujian, as well as Lipu in Guangxi are also nationally well-known processing hubs for preserved fruit, candies, snack food, formulated milk powder, cereals and seafood processing, serving both domestic and export market.

South China is a large consumption base for high quality food. This region comprises two of China's four most developed cities, i.e., Guangzhou and Shenzhen, as well as many wealthy emerging secondary cities including Dongguan, Foshan, Zhuhai, Zhongshan, Jiangmen and

Shantou in Guangdong province, Xiamen and Fuzhou in Fujian province, as well as Nanning and Guilin in Guangxi province, where there is huge demand for high quality food products by a wealthy population. Third tier cities and rural areas in south China, especially in Guangdong and Fujian, have a relatively higher level of development and income, compared to those in the inland region, and residents there will gradually become consumers for high quality food products.

Wealthy southern Chinese consumers are big fans of a wide range of good quality food products for daily consumption as well as gifting, as food has been an important part in the regional subculture. Many common food, even fruit and vegetables, meat, beans and nuts are well perceived by southern consumers of certain particular health benefits, which has been widely used by food manufacturers in new product development and promotion.

1.5.2 East China

The food processing industry is a fast growing sector in the economy of Shanghai and the entire Yangtze River Delta Economic Zone (YRDEZ), thanks to the region's affluence, huge population, sound industry infrastructure, and easy access to seaports. The total value of the food processing industry in the YRDEZ was US\$ 297 million (RMB 2.4 billion) in 2006, the latest full year available data (See table 1.4 for details in respective regions). The numerous food processors in Shanghai, Kunshan (Jiangsu Province), Suzhou (Jiangsu Province) and Hangzhou (Zhejiang Province) can be a good opportunities to U.S. food ingredient exporters.

1.4 Food Processing Industry in YRDEZ by City and Province, 2006

Cities and Provinces	Number of Food Processors	Gross output (million US\$)	Number of Food M'facturers	Gross Output (million US\$)	Number of Beverage M'facturers	Gross Output (million US\$)
Shanghai	179	1,879.3	273	2,728.1	62	1,317.3
Jiangsu	983	8,830.0	300	2,419.5	193	2,926.8
Zhejiang	776	5,057.3	322	2,077.9	276	2,483.8
Total	1,938	15,766.6	895	7,225.5	531	6,727.8

Data Source: *Shanghai, Jiangsu and Zhejiang Statistical Year Books 2007*

Note: "Food processors" in the Chinese yearbook refer to preliminary processing agricultural products into food, and "food manufacturers" refer to more in-depth processed food manufacturing.

Shanghainese spent 36 percent of their disposable income on food in 2006. A growing percentage of that amount was spent on imported products as well as products with imported ingredients, such as dairy products, snack foods, tree nut products and confectionary items. Consumers are willing to pay premium prices for branded products with more variety and higher quality, and they are more receptive to new flavors from overseas countries. Additionally, Shanghainese spend a sizable portion of their income dining out, increasingly at western or chain restaurants that use imported products such as U.S. poultry, pork, seafood and potato products. Chain pizza restaurants such as *Pizza Hut* and *Papa John's* which use American potato products and cheeses, for example, are increasingly popular among the younger generation.

With the fast rise in incomes, a healthy lifestyle concept is building among the affluent urban residents in the YRDEZ, and because of that, a new demand for convenient, healthy, low-fat and fortified food products is expected to grow. Major events including the approaching 2010

World Expo to be held in Shanghai will create additional growth opportunities for HRI and retail players.

1.5.3 North China

North China is home to a significant portion of China's food processing industry with more than 13,117 food processors located in the Special Municipalities of Beijing, Tianjin, and Henan, Liaoning and Shandong Provinces. More than 65 percent of these are classified as agricultural product processors and the remainder as food and beverage manufacturers. Henan, Liaoning and Shandong Provinces have the highest concentration of processors, primarily seafood, meat, poultry, dairy and grain as well as the production and bottling of beer. In the value-added food processing sector, Japanese and Korean operations are dominant in Shandong and several other Northeast China Provinces.

Table 1.5 North China Food Processing Industry at a Glance (2006*)

Categories	Number of Enterprises	Percentage (%)	Total Revenue (million US\$)
Food Processors	8,642	65.9	3,977.5
Food Manufactures	2,820	21.5	1,720.5
Beverage Manufactures	1,655	12.6	1,233.0
Total	13,117	100.0	6,931.0

*Latest available data, exchange rate: \$1= RMB 8.0
Data Source: *China Statistical Year Book 2007*

While China's logistical and cold chain systems improve, underdevelopment of these basic systems continue to impede the region's food industries. Distribution channels and cold chain facilities are somewhat less efficient in North China compared to East and South China. For many food products requiring cold chain facilities, the cost of food and agricultural inputs can increase as much as 2-3 times from the port of entry to final inland destination. This is due to long transportation distances, poor handling and inadequate refrigeration systems. However, expanded warehouse capacity, and improving importer and local agent networks in North China should eventually enable distributors to keep key items in stock despite current long transoceanic lead time and other inefficiencies.

Rapidly changing and increasingly modern, fast paced lifestyles, especially for affluent urban residents, means consumers often prefer to purchase value-added products in supermarkets or hypermarket formats. And, many consumers are migrating from price to quality, meaning value-added products are very much on the rise. Portion control, ready-to-cook, ready-to-eat and drink, ready-to-go meals including meat, seafood, dairy and starch based foods such as noodles, instant rice, and pizza that require minimal preparation effort and time are increasingly being positioned to meet changing consumer needs. Easy to prepare, high quality, nutritious and products generally perceived as safe continue to grow in popularity.

Consumers in the North China region often prefer food products that are starch based. Local trade resources estimate that 1 out of every 3.5 packages of instant noodles, and 5 out of 10 of packages of ham sausages produced in China are made in Henan Province. The largest meat and poultry processor, Henan *Shineway Group (Shuanghui)*, and *Sanquan* the leading producer of frozen dumplings are both located in Henan. Also, there are a variety of other food processors and ingredient suppliers located in this important province known for its flour based foods including organic and soybean flour.

Challenges facing North China food processors are the relatively large number of obsolete manufacturing facilities and technologies employed as well as lack of investment and lack of experienced technical management. In the past, cold chain and logistical systems evolved to meet the demands of mostly frozen cold storage only. However, current market demand for chilled and increasingly environmentally controlled capacities makes many of the facilities described above mostly out of date. Thus, optimization of capital, technology, and technical management are critical to development of reliable cold chain and cost efficient capacities beyond warehousing and refrigerated trucks. With the above said, cold chain and distribution systems continue to evolve and improve with good investment and trade opportunities in this sector. This is particularly true in a number of China's Emerging City Markets, many located in North China, characterized by double-digit GDP growth rates, emerging middle classes, and rising disposable incomes. (See *GAIN CH7403 for more information about Emerging City Markets in China.*)

1.6 Analysis of Product Categories

1.6.1 Oils and Fats

China is a large processor of edible oils, with bulk raw materials such as soybeans produced in northeast China, rapeseed from middle and down stream areas of the Yangtze River, peanuts from Shandong and Henan, sunflower seeds from Jilin, Xinjiang and Inner Mongolia, and cottonseed from Xinjiang, Shandong and Hebei provinces. According *China's Food & Oil Information Center*, total consumption of edible oils in 2007 reached 18.5 million metric tons, and small packaged refined edible oil sales is growing at an annual rate of 25 percent in China.

Driven by rapid commercialization of its meat and feed industries and strong growth in food consumption overall, China's soybean meal and soybean oil consumption have been rising at double digit annual rates since 1999. Many large oil crushing plants were built along the east coast of China, including Dalian of Liaoning Province, Tanggu of Tianjin, Rizhao of Shandong Province, Zhangjiagang of Jiangsu Province, Dongguan of Guangdong Province, and Fangchenggang of Guangxi Province, aiming to take advantage of the easy transportation combined with port facilities and extensive network of railways and highways. There are 47 oil crushing plants, each with a daily crushing capacity of over 1,000 metric tons along China's coast, forming 80 percent of the total crushing capacity in China, with an annual processing capacity of 60 million metric tons. Among them, *Donghai Food & Oil Co.* located at Zhangjiagang in Jiangsu Province, is the world's largest oil crushing plant, with a daily crushing capacity of 14,000 metric tons of soya.

China is the largest export market for U.S. soybeans with over 435 million bushels (11.8 million metric tons) exported during the most recent marketing year, which was 40 percent of all soybean exports from U.S. All imported soybeans are crushed into soybean meal and oil - the meal for animal feed and the oil for cooking.

The import quota for edible oil products will be waived by the Chinese government in 2008; with this action, the import of edible oil is expected to grow, and palm oil will be the leading product driving the growth. Meanwhile, influenced by domestic soybean production and pricing on the international market, imports of GMO soybeans for oil crushing will be difficult to predict.

Distribution of edible oil in the China market has two major patterns: direct sales are more common in first-tier cities including Beijing and Shanghai, where the population is huge and retail outlets are well developed, whereas in second-tier and third-tier cities the oil products reach consumers via distribution channels, such as Wenzhou in Zhejiang Province. In large second-tier cities such as Wuhan in Hubei Province, where there are many hypermarkets, direct sales and distribution are combined to save costs and ensure efficiency.

With increasing disposable incomes in urban areas, more health-conscious consumers tend to eat "healthier" oils such as tea oil, olive and corn oil. These niche markets, though very small, have enjoyed good margins and fast growth.

1.6.2 Dairy Products

Consumption of dairy products in China has steadily grown in recent years due to increasing disposable income, nutritional demand for higher protein intake and expanding retail network. Liquid milk and yogurt comprise of the majority of the dairy products in the market, and sophisticated products such as cheese, cream and products of high value dairy ingredients have very limited presence only in large cities.

Consumption of fluid milk remains at high levels in big cities. Milk powder is losing significance in the dairy consumption market, with only fortified products targeting infants and senior citizens continuing to grow. As the per capita annual consumption of cheese is 48.5 lbs in Europe and 32.5 lbs in the US, while in China the rate is only 0.5 ounce, it is estimated that cheese, with high added value, is the next "growth point" in the domestic dairy market. With the Olympic Games being held in China this year, it is widely predicated that cheese consumption will see dramatic growth in 2008. Yogurt continues to grow at a comparatively high rate thanks to its diversified flavors and perceived health benefit.



Domestic dairy brand emphasizes natural farm on its advertisement.
(Source: ATO Beijing)



Domestic dairy brand emphasizes pure and fresh milk on their milk package.
(Source: ATO Beijing)

Functional milk products are on the rise with growing demand for health and wellness products. Some of these new products include high calcium, collagen, fiber and vitamin E enhanced milk as well as low fat, and cereal fortified milk positioned as beauty products catering to an emerging niche market targeted at women and children. In cooperation with its strategic partner *Danone*, *Mengniu* introduced probiotic ingredients in its mulberry and pomelo flavored milk products in 2007.

Local manufacturers lead the dairy sector in China with Inner Mongolia *Mengniu Milk Industry (Group) Co. Ltd (Mengniu)* topping the list. The company has a wide dairy product portfolio including ice cream and yogurt. In 2007, *Mengniu* invested \$162million (RMB 1.2 billion) in the new high-tech production base, the largest in the world, in Hohhot. With 22 production lines and a daily production capacity of 2,000 tons *Mengniu* is by far the largest. *Yili Industrial Group* owns more than 130 subsidiary companies and branches including ice-cream, and other dairy

products. The *Yili Company* is the official dairy sponsor for the 2008 Beijing Olympic Games.

Another strong domestic player is the Shijiazhuang *Sanlu Group* which specializes in infant formula and baby milk products. In cooperation with *Fonterra*, *Sanlu* developed a first-class dairy operation in Tangshan in Hebei Province. The company imported 5,000 top quality dairy cows from New Zealand as well as used *Fonterra's* research and development expertise to produce high quality raw milk to produce milk powder and baby milk formula in China.

Table 1.6 Top 10 Dairy Companies in 2006

Rank	Company	Location	Retail Value (Million US\$)
1	Inner Mongolia Mengniu Milk Industry (Group) Co., Ltd	Inner Mongolia	2,614
2	Inner Mongolia Yili Industrial Group Co., Ltd	Inner Mongolia	2,298
3	Shijiazhuang Sanlu Group	Hebei	1,279
4	Bright Dairy & Food Co. Ltd	Shanghai	976
5	Danone Group	Multiple locations	923
6	Nestle SA	Multiple locations	342
7	Hunan Taizinai Group	Hunan	271
8	Sichuan New Hope Agribusiness Co., Ltd	Sichuan	264
9	Xuzhou VV Food & Beverage Co., Ltd	Jiangsu	193
10	Beijing San Yuan Foods Co., Ltd	Beijing	174

Source: Euromonitor International 2008

International dairy product players increasingly take a larger role in the market. The *Danone Group* is ranked number five in fluid milk beverage products with a market share by value of nearly 5 percent followed by *Nestle* with over 2 percent. *Nestle* has also been active in powdered milk product development with its *Nestle Hi-Fiber* and *Hi-Calcium Milk*.

With rising raw milk prices and fierce competition among the dairy giants, including *Yili* and *Mengniu* from Inner Mongolia, *Sanlu* from Shijiazhuang, and *Bright Dairy* from Shanghai, breakthroughs in sales are difficult to achieve. Generally speaking, greater market potential for liquid milk, yogurt and powdered milk lies in second-tier cities and rural areas. Restricted by lower income levels and yet-to-improve cold chain distribution channels, however, real growth will be difficult to achieve in the short term in these two market segments. Therefore 2008 will see a relatively steady overall dairy market.

Insufficient domestic milk supply, mostly used for fresh or UHT milk, has created opportunities for imports of dairy ingredients including whey, powder milk, lactose, cheese and butter as ingredients to make ice cream, milk drink, infant formula, chocolates and baked products. The US, as a globally dominant supplier of whey and other dairy ingredients is more competitive than EU, Oceania and South America in terms of prices and available supply to serve the China market. Long-term upward price trends constrain exports to China, though the weakening dollar takes off the edge. Current Chinese standards exclude imports of deproteinized whey for food use. High end niches including de-lactose products, functional and energy products as well as those for performance enhancing, disease recovery are of best prospectus.

(Please refer to GAIN 8605 for more details of the high value dairy ingredients market in China.)

1.6.3 Meat

China's meat processing industry which includes fresh, frozen, canned, preserved and chilled meat products is highly fragmented. *Henan Shineway*, located in Henan Province, enjoys a nearly 20 percent market share for canned, preserved meat, and meat products as well as an 8 percent chilled processed meat market share, making it the largest meat company in China. Other major players include *Yurun*, located in Jiangsu Province and the *People's Food Holding Ltd*, headquartered in Shandong Province. Competition among these three rivals is intense in most first-tier cities, whereas regional players dominate regional markets. Given recent meat supply shortfalls, and rising domestic meat prices combined with an appreciating Yuan versus the U.S. dollar, domestic meat processors seeking meat and meat product imports. Traditional low value pork product imports are no longer able to satisfy the domestic needs of China's expanding meat processing industry.

1.6.4 Bakery

The baking business is booming in wealthy regions, especially in large cities such as Guangzhou, Shenzhen and Shanghai. Improving income levels drive consumers to become more lifestyle focused, and the faster pace of life is making ready-to-eat and prepared foods more accepted. The lucrative business has attracted both foreign and domestic bakery operators. Western style baked items, including breads, cakes, pastries and desserts, are becoming very popular daily items.

Mooncakes, Chinese delicacies enjoyed by families in the Mid-Autumn festival season in mid-to late September and the following National holidays, have become the biggest revenue generators during a year for bakeries in China. Sales for mooncakes robustly increase as families, friends and associates seek out ever more generous gifts during this important festive season. Record sales in CY 2006 of US\$ 1.4 billion plus growing hunger for trendy new style mooncakes with innovative fillings mean there's a niche market for U.S. ingredients. However, the chief challenges are price and ingredient awareness. They need to be combined to maximize taste and profit. (Refer to GAIN CH7624 for more details on the China mooncake market.)

Though traditional Chinese pastries such as moon cakes still dominate, consumers are becoming more sophisticated and demanding for greater varieties and quality of bakery products. Premium bakery chains continue playing a leading role in distribution, product innovation with fierce competition. Regional bakery chains are the most influential operators in respective territories, and there is no national chain yet.

While veteran chain stores such as *Marco Polo* in Shanghai, *Maxim's Group* and *Queens Cake Shops* in Guangzhou, enjoy consumer loyalty, thanks to their consistently high product quality, upscale newcomers like *Bread Talk*, *Yamazaki* and even



Demonstration of ingredient application at the Bakery China 2008 trade show
(Source: ATO Guangzhou)

Starbucks Coffee and *Circle K Convenient Stores* are trying to gain market share by introducing innovative flavors, interesting product names, on-site baking, and eye-catching store images.

China is one of the most promising potential markets for U.S. bakery ingredient exporters. Making products with high quality ingredients is a way that high-end bakeries use to differentiate themselves from competitors, and thus create substantial demand for high quality ingredients. A wide range of imported bakery ingredients, including dried fruits, almonds, hazelnuts, raisins, butter and cheese are frequently incorporated in bakery goods by high-end bakeries, aiming to enhance nutrition and improve appearance with the consequence of bringing the products higher margins. Compared to U.S. exporters, EU counterparts more aggressively promote their ingredients and have taken a leading position in the market.

1.6.5 Baby Food

Infant formula milk powder, dried baby food (rice powders etc.) and prepared baby food (packaged foods in cans and jars) constitute the major baby food market. The spread of retail outlets, improved cold chain and distribution systems, and increased ownership of refrigerators per household are contributing to the growing consumption of more diversified baby food products. In 2007, sales of baby food reached 3 billion US\$ (RMB 23 billion), up 28 percent from the previous year¹. Baby foods market in China has grown 153 percent since 2002, and the sales are expected to grow at over 20 percent annually in the next five years.

Approximately 20 million babies are born in China every year. Statistics show that the population of infants from newborn to 4 years old is 80 million. The family plan imposed by the Chinese government, allowing most Chinese families to have only one child or face stiff fines, ensures that more care and attention are lavished on those children.

With increased disposable incomes, young Chinese couples demand safer and better quality baby foods, with less sensitivity to price. This leads to strong growth of the overall market for baby foods. Newcomers, both domestic and overseas companies, continually enter the market, pushing the demand with many new and increasingly sophisticated products for babies.

Spending per child is on the rise, as consumers are able to afford higher quality and more expensive products. In Shanghai, for example, the value of baby food sales reached nearly US\$181 million (RMB1.5 billion) in 2004, with spending per child at US\$ 12.55 (RMB 104.2), an increase of 63 percent since 1998.

Increasingly, working mothers influence the baby food industry. Statistics show that nearly 80 percent of all working women are mothers in China, of newborn to 16 year old children. Working mothers help maintain household incomes at higher levels, but they have less time to prepare fresh food. All these factors create opportunities for packaged baby foods. What's more, the institutional market for baby food products is growing, as nurseries and childcare institutions are mushrooming, and those with better training programs and better food and care always attract busy working parents.

¹ *Baby Food – China*, Enromonitor 2007

Table 1.7 Market size of different sectors of baby foods, 2006-2007

Sectors	2006 (million US\$)	2007 (million US\$)	Growth (%)
Infant Formula Milk Powder	1,980.6	2,539.5	28.2
Prepared Baby Food	28.9	36.9	27.7
Dried Baby Food	268.1	328.6	22.6
Total	2,277.7	2,905.0	27.5

Data Source: Euromonitor

Infant formula milk powder represented 87.4 percent of the total market value in China in 2007, the fastest growing product category. Although breastfeeding has been actively promoted by the government and health authorities, working mothers having to return to work after their maternity leave (normally 90-120 days, even up to 170 days) in urban areas are hence no longer able to breastfeed their babies. Thus, infant formula milk powder becomes the best alternative. In addition, strong advertising campaigns by the infant formula giants such as *Nestle* advertise that the added nutrients, minerals and vitamins in their products help babies' brain and eye development. Foreign brands such as *Nestle*, *Wyeth*, *Similac Advance*, *Ausnutria*, *Dumex*, *Anmum*, *MeadJohnson*, *Primavita*, *Ausmeadow*, and *Good Health* share 80-90 percent of this market, while *Yili* from Inner Mongolia and *Wandashan* from Heilongjiang are the biggest domestic brands.

Dried meals and canned foods for baby growing, with flavored rice powders the most significant part of the dried meals category, and mixed vegetables, fruit, fish and meat are developing into much more diversified flavors. *Heinz* and *Nestle* entered the China market in the 1980's and since then have built up high awareness among their target consumers. The domestic brand *Beingmate* created in early 1990's, together with *Nestle* and *Heinz*, hold more than 50 percent market share. Imported products such as *Gerber's* baby food, dominate the high end market and have cultivated their own loyal consumers. Attracted by huge potential, newcomers such as *Eastwes* and *CEVO* have entered into this market of fierce competition.

Post estimates that the baby food market will continue its fast growth, with rising incomes and receptiveness of China's younger generation to more sophisticated products. Thanks to the perceived status of the only child in the family, the baby food market is much less price sensitive, especially in affluent areas. Brand awareness, which is the guarantee of quality and safety, is key.

1.6.6 Beverage

China has become the largest brewer in the world. Beer is the most popular alcohol beverage across China, outperforming the conventional Chinese liquor. In North China where China's top four beer brands' are headquartered, beer production is among the most significant processing industry. Key brewing ingredients including hops and malt are in great demand, due to limited domestic supply, and brewers pay high prices for imports mostly from Germany, France, Australia and the U.S. As beer demand continues increasing, demand for brewing ingredients will also increase.

According to *Euromonitor*, *China Resources Breweries Ltd. (CR Breweries)* which owns the *Snow Beer* brand, occupies the number one position in terms of national market share at 15.8 percent, followed by *Tsingtao* with 13.9 percent, and *Yanjing* at 10.5 percent as well as *Harbin Beer* with a 4.4 percent national market share. Based in Beijing, *CR Breweries* is a

joint venture between the *China Resources Enterprise* and the *SABMiller Group* (world's second largest brewer). *Snow Beer* is one of the 30 leading beer brands under *CR Breweries*. US global beer giant *Anheuser-Busch*, owns a significant share of *Tsingtao Beer* (27%) and *Harbin Beer* outright. These new investments in beer have benefitted China's beer producers as growing affluence in China drives expanding beer consumption. Based in Beijing, *Yanjing Beer* remains one of the only brewers in China not teamed up with an international partner or arrangement. Yanjing Beer occupies a whopping 50 percent market share in North China, and something on the order of greater than 90% of the Beijing market, as well as operating the single largest beer manufacturing facility in Asia.

Promising demand for fruit juice and juice drink are quickly emerging in urban areas. In general customers aren't yet fully aware of 100 percent juice which holds a small niche market due to its relatively high prices and consumers' limited awareness. Starting from a small base, fruit juices and juice drinks are of promising sales potential in supermarket and hypermarket, as health-concerned consumers are shifting their preference from carbonates to juice beverage, including pure juice, juice drinks, nectars with pulp and fiber; NFCs (not from concentrate). The increasing demand of juice products is creating opportunities for both imported juice products as well as the juice concentrate, due to the limited domestic supply. (Please refer to GAIN 8603 for more details on the juice market in China.)

1.6.7 Dried Fruit and Nuts

Chinese consumers have long been big fans of dried fruit and nuts, especially because of health attributes. Most dried fruit and nuts are eaten as snacks, though these as food ingredients are gradually increasing in the bakery, confectionary and food service sectors. Though there are no official statistics on dried fruit and nuts consumption in China, industry sources indicate a nationwide steady increase, based on increasing new food varieties with dried, preserved fruit and nuts as ingredients.

Most dried fruit products are made with domestically grown fruit ranging from deciduous and tree fruit to citrus and tropical fruit. Dried raisins, plums and tropical fruit (mango and pineapple) have been imported to China, albeit in limited volume and mostly available in affluent urban area.

Domestic peanuts accounts for the largest share of nut consumption, while pistachios and almonds are the most popular imported nuts. Chinese consumers enjoy cracking the shells so many nut snacks, especially less expensive ones, are in-shell. Nuts of good quality at high prices are sold in wealthy coastal areas, whereas less expensive nuts are more popular in less developed areas.

Most dried fruit and nuts are consumed as snacks. In recent years, an increasing niche has emerged in the fast growing bakery and confectionary sector, which features dried fruit and nuts as ingredients in various forms to make a wide range of products from cakes and breads to candies and biscuits. Due to limited knowledge of U.S. dried fruit and nuts and their applications, technical assistance and product recipes are helpful in promoting the nuts ingredients to the high end bakeries and confectionary makers.

Price is sensitive and critical for nuts and dried fruit



Dried fruit snacks in a supermarket
(Source: ATO Guangzhou)

consumption in China. Products from the US are often more expensive than those from China or other countries, which prohibits consumption of U.S. products by both the end consumers as well as the food manufacturers. Some manufacturers or bakeries for cost concerns substitute ingredients, for example, almonds, in their product recipe with less expensive ingredients such as peanuts. Educating Chinese buyers about the value that the U.S. nuts add to final products, is a way to convince Chinese buyers and users to use high quality U.S. ingredients instead of less expensive ingredients of inferior quality. The import volume versus price of almonds in 2007 clearly illustrates the price sensitiveness in China market.

Severe IPR infringement is still a threat for U.S. dried fruit and nuts products in China. In general, the high quality of U.S. dried fruit and nuts are well perceived by Chinese consumers. However, end consumers lack the knowledge to distinguish the U.S. products from those originated from other countries. This has created substantial opportunities for counterfeits which claim to be U.S. but indeed made of ingredients from another country.

Counterfeits together with consumers' limited knowledge about U.S. products can badly damage the U.S. industry in the long run. Take pistachios as an example: For the past five years or longer, bleached pistachios from Iran have taken over the leading share from non-bleached but more expensive U.S. counterparts in China, simply because of price.

(Refer to GAIN CH 7071 and 7081 for more market information on dried fruit and nuts in China.)

1.6.8 Confectionary

The confectionary sector in CY 2007 grew 7 percent in sales to US\$ 5.4 billion (RMB 41 billion) from the previous year¹. Sugar confectionary accounts for most of the confectionary products with moderate growth, and chocolate products had a much faster growth from a comparably small base.

Sugar confectionary is moving to maturity. Pastilles, gums, jellies and chews continue to increase despite slower growth in other categories. Unit selling prices remains stable despite increasing cost of raw materials. New product development is a strategy to compete in the market. So is focus on the real fruit juice content as it adds nutrition.

Chocolate confectionary, starting from a small base, has quickly grabbed market share from sugar confectionary. Premium products are the focus in new product development, as companies heavily promote high quality cocoa content in the products. Chocolate products will continuously gain share from the sugar candies. Due to lack of chocolate culture in China, chocolate products face competition from many other snacks that have well perceived by consumers.

Chocolate tends to be eaten more frequently by children and females. Chocolate in big cities such as Beijing, Shanghai and Guangzhou sell well. Sales in second and third tier cities will witness dramatic growth. Many not only buy



*Sunkist candies made by a contracted Chinese company
(Source: ATO Guangzhou)*

¹ *Sugar Confectionary – China and Chocolate Confectionary – China*, Euromonitor, 2007

chocolates for their own consumption but also for gift giving which strongly drives demand.

Milk chocolate is still the most popular flavor among Chinese consumers. Dark chocolate with high percentage of cocoa is mostly purchased by sophisticated customers in China and tends to gain more market share with those conscious about product quality and functional benefits. Sugar free chocolate will be another favorite food product to avoid diabetes.

China's existing standards for candy product manufacturing are not clear and do not match international standards. There are a lot of discrepancies about category classifications and sub-categories. The various inspection methods applied in different cities also led to different results. The industry calls for update and revision on the current standards.

1.6.9 Seafood

China is the world's largest seafood processor, thanks to low labor cost and economies of scale. It is also the largest farmed fish grower in the world. Farmed fish production exceeds the wild catch. China also tops the seafood exports ranking in the world. China is also the largest producer and exporter in the world of tilapia and shrimp, most of which is produced and processed in Guangdong province in South China. Domestically produced and imported seafood is filleted, de-boned and fried or frozen and turned into a growing varieties of value-added products for exports to many countries, including US, Japan, EU and Russia.

Shandong and Liaoning provinces in North China process the most seafood in the country, followed by Guangdong and Fujian in South China, and Zhejiang in East China. Processed seafood is mainly for export. Many processed items such as eels, shrimps, prawns, yellow croaker, tuna, scallops and tilapia were exported to Japan, Korea, Australia, Russia, Canada and United States. In 2007, China imported \$2.4 billion of fishery products from the US, 13 percent share of China's total seafood imports, with estimates as high as 85 percent of these products used for processing and re-export.

Seafood processing is one of North China's major food processing industries which is mostly concentrated along the coastal cities of the Bohai and Yellow Seas, especially in Shandong and Liaoning provinces. Based on Post participation in past China Fisheries Expos held in Qingdao and Dalian, a growing seafood processing industry in North China continues to evolve with Qingdao the major destination for such processing. However, only 4-5 years ago Dalian held the top ranking and still ranks number two in China.

South China leads the production and processing of eel, white shrimp (also called prawn) and tilapia. Fujian is the largest processor of eel in China, with packaged exports valued at \$.7 billion, mostly to Japan and a limited amount to Asian communities in the States and Canada. Japan used to be the location for eel processing. For cost concerns, the processing had later been moved to Taiwan before it was eventually relocated to China. White shrimp is mostly farmed in Guangdong, Hainan and Guangxi provinces, and tilapia mostly comes from Guangdong, Fujian, Guangxi and Hainan.

Food safety became a hot issue for Chinese seafood industry in 2007. Reportedly significant amounts of carcinogens and contaminants were found in several species of farm-raised fish and shellfish in China. In June 2007, U.S. Food and Drug Administration (FDA) issued an import alert, though not an outright ban, on farm-raised catfish, basa, shrimp, dace and eel from China, because of numerous cases of contamination with drugs and unsafe food additives. According to FDA, certain Chinese aquaculture products exported into the United States contained illegal substances that are not permitted in seafood sold in the United States, such as unapproved veterinary drugs. Many Chinese exporters were concerned about future seafood exports to the U.S. market. Despite such legitimate issues with certain Chinese seafood products, they only accounted for a small fraction of China's seafood export.

Chinese seafood exporters are challenged by anti-dumping tariffs ranging from zero to over 100 percent on their exports to the US. Since imposing the tariff, Chinese shrimp exporters have lost significant business.

Coastal provinces in China have higher seafood consumption than those in the inland. Additional supply resulted from the restricted export to US has lowered the shrimp prices in domestic market which in turn boosted the domestic sales. Surging pork prices also stimulates the seafood demand.

1.6.10 Ice Cream

Ice cream sales in 2007 increased 10 percent to US\$ 4.6 billion. Ice cream is becoming more of a snack or dessert rather than consumed only in summer. Sales prices in 2007 rose because of the increasing prices of dairy ingredients, sugar as well as oils and fats. Rich and milky types of products are generally preferred. Consumers prefer flavor over health and wellness. High-end ice cream may be used as a mean to feature a variety of good quality dairy ingredients, dried fruit and nuts.

1.6.11 Quick Frozen Products

Thanks to the improvement of cold chain infrastructures and increased ownership of refrigerator per household, as well as higher family incomes and decreased time to cook among middle-class consumers in urban areas, the quick frozen products sector in China has grown at an average rate of over 20 percent since early 2000s. Increasing affluent consumers, especially urban residents, purchase frozen foods for convenience and access to a variety of products. Ninety percent of frozen food products are consumed by families, via distribution in the retail sector. Distribution channels to the HRI sector have not yet been developed. Most consumers are working mothers and single white-collars in first and second tier cities.

According to *China Institute of Food Science and Technology*, there are 3,000 quick frozen food product manufacturers in China in 2007, making dumplings, buns, pancakes, glutinous rice dumplings and other frozen desserts. Famous brands are *Synear*, *Sanquan*, *Longfeng*, *Haibawang*, *Taixiang*, *Jiayuan*, and *Haodangjia*. Manufacturers are mainly located in north China, especially Henan province. The top six manufacturers held nearly 60 percent share of the market in 2007. In Henan, the top base of quick frozen foods production, over 80 percent of the manufacturers were phased out of market during 2000-2006, owing to fierce competition. However, the winning 10 manufacturers occupied around 40 percent of the China quick frozen product market in 2006.

The promising industry has seen an investment fever in recent years. Large-scale meat processors including *Shineway*, *Jinluo*, *Yurun*, *Zhongpin* have set up subsidiaries specializing in quick frozen food products. Some dairy giants in China also joined the competition aiming to share a piece of the ever growing “cake”. Frozen dumplings produced by Mengniu, the second largest dairy giant in China have been distributed throughout the country.

Local firms have made considerable efforts to attract investment and expand fast. Some successfully export their products to overseas markets such as Japan, Korea and even the United States. Some are listed at the stock market. In 2006, *Henan Syneer*, the frozen food industry's top performer based in Zhengzhou, Henan province was successfully listed on the *Singapore Stock Exchange*, and in 2007, *Sanquan*, another famous brand also based in Henan, got listed on the *Shenzhen Stock Exchange*. The *2008 Olympics* even has an official dumpling supplier – *Syneer*. With annual production of over 300,000 tons, *Syneer* has become the market leader, respectively capturing a 19 percent and 20 percent share in the categories of frozen desserts and other frozen foods products.



Retail package of hand-made quick frozen dumplings
(Source: ATO Beijing)

Encouraged by the promising prospect of the market, international food firms including *Katokichi* from Japan, and *General Mills* from the US came to China to set up their joint ventures or wholly-owned companies. In 2006, *General Mills* invested US\$ 13 million in Shanghai to produce frozen dumplings and wonton, targeting the upper market. *Wanchai Ferry*, the famous brand owned by *General Mills*, has dominated the high-end market and racked up sales of US\$ 18 million in 2006, accounting for 33 percent of the market in Shanghai and over 50 percent in Guangzhou.

While bringing challenges, foreign manufacturers have expanded the frozen food product range by adding new varieties such as frozen pizzas and fries to the traditional best sellers of dumplings, sticky rice cakes, buns and frozen beef/pork/fish/shrimp balls. Though only taking a small share in the market, these new products are gaining popularity among young Chinese consumers.

The industry also faces challenges. Key issues include distribution problems arising from less efficient logistics system, underdeveloped cold chain infrastructure, fragmented market segments, food safety concerns generated from food poisoning scandals, and rising cost of both raw materials (edible oil, flour, pork) and operations (listing charges at retail outlet). In good news for consumers but adding cost for struggling manufacturers that intend to survive at the low end of the market, the Chinese government has required since 2007 that all frozen food products must be packaged, which has driven all unpackaged frozen dumplings from retailers.

Consolidation is taking place in the industry. While small companies are forced to shut down, bigger competitors including *Syneer*, *Sanquan* and *Wanchai Ferry* are rapidly growing. With the continuing urbanization and increasing affluence of Chinese consumers, Post believes that there is immense room for growth in the coming years for the emerging quick frozen food sector in China.

1.7 Market Opportunities and Challenges

Opportunities	Challenges
China is the world's largest food market of large number of middle class with increasing disposable incomes. It is also a large processor of many food categories to supply both domestic and export markets. China's economy is large enough to survive setbacks that hurt others.	Fragmented markets in a geographically large nation with underdeveloped logistics and infrastructure as well as cold chain system. Most live in less developed rural areas.
Fast growing food industry, together with the retail and HRI sectors, create great potential for food ingredients.	Underdeveloped cold chain and lack of expertise in food storage and distribution hamper distribution and storage of temperature sensitive and perishable products.
Upscale food makers eagerly look for high quality ingredients that add value to their products.	Increasing competition among ingredients from various origin
Food is an essential part of Chinese culture and social life.	Consumer preference varies widely from region to region. In general awareness of many U.S. food ingredients and its application is low.
A large number of emerging city markets out of primary first tier cities offer tremendous opportunities for further growth.	Food processing, retail and HRI sector as well as distribution channels in less developed area lag far behind those in the affluent coastal region, which hamper further penetration.
Rapidly weakening dollar makes U.S. products more competitive in this price sensitive market.	Increasing commodity prices and logistics costs offset depreciation of the U.S. dollar.
WTO entry leads to lower tariffs and import barriers, market and legal reform, and increased access for distributors.	Increased access for imports has resulted in greater competition from other exporting countries. TBT and SPS issues impact trade.
Cost advantage makes China a good base for value-added processing.	Workers need substantial training. Operation cost significantly increases due to the increasing cost on labor, fuel, transportation and raw materials.
Fast development of ports in various parts of China provides more entries for products entering China	Logistics and distribution channel in newly developed area still lag.
Increasing concerns about food safety and health creates more opportunities for high quality ingredients	Tightening inspection and conflicting standards forms barriers for imports.

Opportunities	Challenges
Many U.S. products and brands, such as California pistachios, <i>Budweiser</i> , <i>Coca-Cola</i> , <i>M&Ms</i> , <i>Snickers</i> , <i>Campbell's</i> , <i>Heinz</i> , <i>Wrigley's</i> , and <i>Pringles</i> have good reputation in China.	Infringement of intellectual property rights remains a serious concern in China.
Leading food makers are more likely to use imported ingredients to develop new products.	Competitors targeting a lower end segment may use less expensive ingredients as substitute
Upcoming major international events including 2008 Olympic Games in Beijing, 2010 World Expo in Shanghai and 2010 Asia Games in Guangzhou provide ample opportunities to promote food products.	Promotional expenses could be expensive during the event. Also the influence of the event will fade once finished.
Chinese consumers spend more than one-third of their disposable income on food and beverages. Higher living standards, health education drive consumers to demand better quality, more variety in new diets.	Chinese consumers are price-sensitive: imported products have difficulty competing with domestic substitutes on price.
Urbanization and changes in living styles favor consumption of more processed food.	Basic agricultural production is not well integrated with commercial food processing sector.
High-income earners favor products that can improve the quality of life, and willing to pay premier price	Consumers have limited awareness and knowledge of new products. Limited availability of high-end products makes it less accessible.
Imported goods are generally regarded as high in quality.	Imports are regarded as expensive. Price-sensitive consumers are less willing to buy imported products without knowing the value.

1.8 Outlook for the Food Processing Industry in China

Despite setbacks from food safety scandals and surging prices, Post sees healthy development in China's food processing sector. Steady economic growth, growing number of consumers with increasing disposable income, strong demand for food of good quality, nutrition and diversity from, as well as change of life style and food consumption patterns jointly pull the growth of the food industry in China.

With a number of food product scares related to China over the past several years, consumers continue to seek food and beverage products perceived as safe and of high quality. Often imports or products containing imported food products or ingredients are perceived by consumers as higher or superior quality to local ones.

The 2008 Olympic Games in Beijing represents a significant opportunity for the food service and food processing industries given strict food safety standards being implemented, and more importantly enforced. This development will no doubt have both short and long term ramifications. Domestic processors are in a strong position with other country suppliers for a

variety of products including frozen French fries, dairy, meat and seafood products as well as food ingredients.

The upcoming Beijing *Olympic Games* has generated tremendous expectation from the food industry. The event, long before its commencement, has become an exciting theme for many large domestic and foreign food companies who aim to aggressively further increase their market share and to extend the product lines by grasping the nationwide passion on this unprecedented event in the country. Many food advertisements emphasize the linkage between the products and the Games, sports and athletes.

In addition, the event provides a great opportunity with challenges for Chinese food industry to move forward in many aspects such as quality control, logistics and cold chain operation, food safety and hygiene and product versatility which will have longer term impact even after the event.

Despite fading enthusiasm after the event, the *Olympic Games* greatly influence the food industry in China. Other upcoming international events including the *2010 World Expo* in Shanghai as well as the *2010 Asia Game* in Guangzhou will similarly further push the food processing industry to a higher level in the similar way.

Since the Year 2000, China's food processing industry has grown at double digits annually. The country's *11th Five Year Plan* covering the period, 2006-2011, has encouraged and set the stage for food processing industry's development. According to the *Plan*, the food processing industry will focus on:

- food safety as a top priority;
- meeting the growing demand for healthy and nutritionally sound food and beverage products;
- meat processing and cold chain logistics and facilities improvements;
- convenience and variety of food will increase and expand; and
- advanced technologies in the food processing industry will be encouraged.

The plan defines these key sectors:

- Grain processing
- Edible oil processing
- Fruit and vegetable processing
- Meat processing
- Fishery and seafood processing
- Dairy processing
- Beverage production

II. Roadmap for Market Entry

2.1 Entry Strategy

Market knowledge and relationship with local partners are crucial to succeed in the diverse and fragmented China market. New entrants must conduct comprehensive market research to thoroughly understand the market and potential for their products, based on which entry strategies are formulated. Visiting in person is important to develop good business relationship with Chinese partners and clients.

Despite the huge potential in China, lack of understanding of the market has resulted in failure by many foreign companies. U.S. exporters should consult the Agricultural Trade Offices (ATOs) in Guangzhou, Shanghai, Beijing, Chengdu and the soon to open ATO in Shenyang for a better understanding of the respective regional markets in China. *(Refer to Section VII at the end of this report for ATO contact information.)*

Many Chinese traders and ingredients users don't know about U.S. ingredients and application. Exporters should educate potential clients with product knowledge and closely work with clients to promote ingredients and develop recipes of final products.

Exporters often find it advantageous to work with Chinese distributors who have well established distribution channels, rather than spending tremendous resources to establish their own channels. To work with such distributors, exporters can quickly enter the market with limited financial and personnel resources via the distributor's established channel. Reputed distributors with their in-house technician team, constantly providing end users with value-added technical assistance will greatly help the sales of products in long term.

2.2 Distribution

2.2.1 Distribution pattern

Coastal affluent regions in China, including Guangdong, Shanghai, Jiangsu, Zhejiang, Shandong and Beijing, accommodate most of the food enterprises in the country. These regions are also the key markets for processed food consumption, due to their well-developed economy, large population and high disposable income.

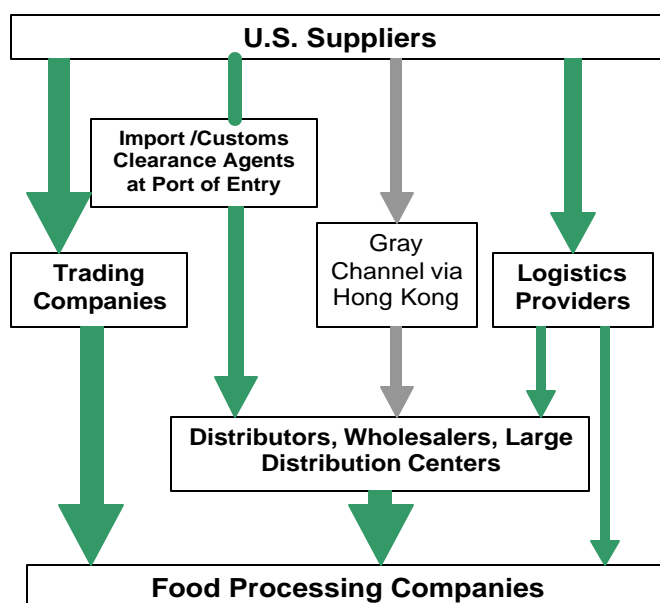
Some less developed provinces, such as Fujian and Guangxi in south China, Henan, Inner Mongolia and Liaoning in northern China, have quickly developed food processing sectors and established distribution network across the country.

The development of transportation and distribution channel widely varies from region to region. Infrastructure and transportation system are well developed in coastal area of southern, eastern and part of the northern China, but lag far behind in the inland region in central, western, and most of the northern part of the country. The catastrophic earthquake in May 2008 badly damaged the infrastructure in Sichuan province which serves as the transportation hub for the southwestern China.

Most imported food ingredients enter into China via main seaports along the coast, namely Guangzhou, Shenzhen, Xiamen in southern China, Shanghai in eastern China, Qingdao, Dalian and Tianjin in northern China. For years, ports in southern China have served as the main entry for imports of many food products, especially poultry, fruit and nuts, cereals, soybeans and dairy products. South China also serves as a distribution hub for imports of many food ingredients to the rest of the country (Refer to GAIN CH7609 *Bustling Ports in South China* for more details). As a result of the rapid development of port facilities in Shanghai, Qingdao, Dalian and Tianjin, significant increases of imports via these ports have been recorded.

Distribution networks of imported products typically consist of traders/importers, logistics providers, customer clearance agent, distributors and wholesalers. The chart below (Figure 2) illustrates the flow of products across the distribution channel, and appendix 1 and 2 elicit the parties involved in the distribution as well as the required documentation.

Figure 2. Distribution Flow Chart



Source: ATO Guangzhou

2.2.2 Cold Chain

The underdeveloped cold chain in China cripples distribution of food products that need temperature control. In developed countries such as the United States, Japan and European countries, over 80 percent of perishable food products such as meat, fruits, vegetable and dairy products are transported in refrigeration, but only 15 percent in China with most concentrating in primary large cities. Lack of technical know-how, less efficient equipments and well-trained staff working along the cold chain have led to high spoilage of food products. Food industry in the country has initiated efforts to encourage cold chain development and improvement. Despite relatively well-developed cold chain system in first tier cities, it will take another 5-10

years to establish such systems in secondary and third tier cities where the large population of emerging middle class will generate substantial demand for high quality food.

2.2.3 Potential of Air Freight

Many have thought about taking advantage of the empty cargo space of back-haul airplanes to deliver U.S. food and agricultural products to China. Though air cargo bound for China is growing, food and agricultural products only make up a fraction. The potential of air freighted food products is determined by demand in the market which currently lies on the high-end niche.

Air cargo industry believes that in the next 15 years, mainland China will have the fastest growth of airborne cargo in the world at an average annual growth rate of over 10 percent, compared to 6 percent for the world. In the next couple of years, high value products including electronics, medicine and pharmaceutical materials, luxury fashions and jewelry will comprise the bulk of the cargo while food and agricultural products will only account for a limited share. The expensive air freight limits the amount of food and agricultural products that is air-shipped. High value bioactive food ingredients and perishable fruit may be potential sources of airborne food cargo from the US.

2.3 Company Profile

Again, the food processing industry in China is fragmented. Leading companies hold a relatively small share in the market, and the rest is divided by numerous small companies. Table 2.1 illustrates that top 20 packaged food manufacturers together hold only 27.9 percent of the retail market share. Top players in the market gradually increase their share, partially due to economies of scale and better performance by top companies.

Table 2.2 lists the top two companies in respective sectors. Although the top two companies in each sector may account for over 50 percent of the market, there are usually many other enterprises in the sector that hold part share, which together account for a significant percentage of the market. As the industry is further broken down into smaller sub-sectors, clear leaders prevail in some cases, but not all.

Table 2.1 Package Food Top 20 Players by Market Share (2002-2006*)

Retail Value RSP - %	2002	2003	2004	2005	2006
Inner Mongolia Mengniu Milk Industry (Group) Co., Ltd.	0.6	1.3	2.1	2.9	3.9
Inner Mongolia Yili Industrial Group Co., Ltd.	1.4	2.0	2.5	3.0	3.5
Kuok Oils & Grains Pte. Ltd.	1.2	1.8	2.0	2.2	2.5
Ting Hsin International Group	2.3	2.5	2.5	2.5	2.4
Shineway Group	1.5	1.4	1.5	1.8	2
Shijiazhuang Sanlu Group	1.1	1.3	1.5	1.7	1.7
Danone, Groupe	1.5	1.6	1.6	1.6	1.6
Hebei Hua Long Food Co., Ltd.	0.7	0.9	1.0	1.1	1.3
Nestlé SA	1.3	1.3	1.4	1.2	1.2
Bright Dairy & Food Co., Ltd.	-	1.3	1.3	1.2	1.2
Uni-President Enterprises Corp	1.1	1.1	1.0	1.0	1.0
Want Want Group	0.8	0.8	0.8	0.8	0.9
Wrigley Jr Co, William	0.4	0.6	0.8	0.8	0.8
China National Cereals, Oils & Foodstuffs Imp & Exp Corp (COFCO)	0.4	0.6	0.7	0.8	0.7
People's Food Holding Ltd.	0.6	0.6	0.6	0.6	0.6
Shandong Luhua Group Co., Ltd.	-	0.5	0.4	0.5	0.6
Shanghai Liangyou Group Co., Ltd.	0.1	0.3	0.4	0.4	0.5
Baixiang Food Group	0.5	0.5	0.5	0.5	0.5
Guangdong Strong (Group) Co., Ltd.	0.4	0.4	0.5	0.5	0.5
Foshan Haitian Flavouring & Food Ltd.	0.3	0.4	0.5	0.5	0.5
Total	16.2	21.2	23.6	25.6	27.9

* Latest available full year data

Source: Euromonitor International

Table 2.2 Processed Food Retail Sub-Sector Market Share (%)

	2002	2003	2004	2005	2006*
Baby food					
Royal Numico NV	0.7	0.7	0.6	0.3	12.0
Bristol-Myers Squibb Co.	11.1	11.2	11.4	12.1	11.4
Bakery products					
Kraft Foods Inc.	2.4	2.5	2.5	2.6	2.6
Artal Group, Belgium	2.0	2.0	2.1	2.2	2.3
Canned/preserved food					
Shineway Group	10.7	11.4	12.7	15.2	16.1
People's Food Holding Ltd.	4.9	4.4	4.9	5.4	5.7
Chilled processed food					
Shineway Group	2.7	2.8	3.3	5.6	7.3
China Yurun Food Industry Group Co., Ltd.	0.8	0.9	1.9	2.3	3.2
Confectionery					
Wrigley Jr Co., William	4.4	6.6	8.6	9.5	9.7
Perfetti Van Melle Group	3.4	3.5	3.6	3.8	4.2
Dairy products					
Inner Mongolia Mengniu Milk Industry (Group) Co., Ltd.	3.7	7.3	10.7	13.2	16.8
Inner Mongolia Yili Industrial Group Co., Ltd.	7.8	10.4	12.4	13.7	14.8
Dried processed food					
Ting Hsin International Group	19.6	21.1	21.0	21.0	20.5
Hebei Hua Long Food Co., Ltd.	7.6	8.8	10.5	11.6	13.1
Noodles					
Ting Hsin International Group	23.0	24.9	24.9	24.8	24.2
Hebei Hua Long Food Co., Ltd.	8.7	10.0	12.1	13.3	15.1
Oils and fats					
Kuok Oils & Grains Pte. Ltd.	30.9	38.5	38.7	40.2	40.2
China National Cereals, Oils & Foodstuffs Imp. & Exp. Corporation (COFCO)	8.3	10.3	10.8	12.3	10.0
Pasta					
Dongguan Humen Ri Long Food Factory	15.0	15.3	14.3	14.0	14.0
Zhuhai Yat Hing Food Ltd.	10.5	10.7	9.4	9.2	9.2
Ready meals					
Danone, Groupe	18.9	18.5	17.6	16.7	16.3
Xiamen Yinlu Food Co., Ltd.	16.4	16.6	16.2	15.6	16.0
Sauces, dressings and condiments					
Foshan Haitian Flavouring & Food Ltd.	4.2	5.2	7.1	7.7	8.0
Lee Kum Kee Co., Ltd.	2.8	3.2	3.6	4.0	5.1
Sweet and savoury snacks					
Want Want Group	6.7	7.5	7.1	7.9	8.4
Guangdong Strong (Group) Co., Ltd.	5.5	5.7	6.1	6.8	6.8
Soup					
Unilever Group	33.0	33.2	34.0	33.5	33.3
McCormick & Co., Inc.	12.0	12.0	12.4	12.6	12.8
Spreads					
Wang's Bee Garden Co., Ltd.	6.9	8.2	11.5	15.1	15.6
QP Corp.	4.9	4.8	4.9	5.1	5.3

* Latest full year data available

Source: Euromonitor Market Database

2.4 Sector Trends

Foreign investments continue to grow in the food industry, especially in food manufacturing and beverage manufacturing which require more sophisticated operation and technical know-how. In CY 2006, foreign funded food business in China recorded annual sales of US\$ 85.9 billion, a 28 percent increase from the previous year (Table 2.5). Compared to the domestic enterprises, foreign funded companies in general perform better due to the advantages in technology, management, quality of input and final product as well as the sales and marketing. Foreign funded enterprises are the market leaders in many sectors, including baby food, bakery products, confectionary, dried processed food, oils and fats, noodle and pasta. Most of the large international food manufacturers including *Danone, Cadbury, Cargill, Hormell, Purdue, Nestle, Kraft, Pilsbury, Yum!, Campbell's, Kellogs, Smithfield, McCormick,* and *Heinz*, have well established their operation in China to have a cut of this huge market. Table 2.5 shows the growth of foreign funded food enterprises in China.

Table 2.5 Foreign Funded Food Industry (as of 2006*)

	Enterprise Number			Sales Revenue (billion US\$)		
	2005	2006	YY increase %	2005**	2006***	YY increase %
Food Processing	2,130	2,321	9.0	37.5	45.1	20.3
Manufacture of Foods	1,259	1,385	10.0	16.8	22.7	35.0
Manufacture of Beverages	569	649	14.1	12.9	18.2	41.1
Total	3,958	4,355	10.0	67.1	85.9	28.0

* Latest full year data available

**US\$ 1=RMB 8.2

*** US\$ 1 = RMB 8.0

Source: *China Statistical Yearbook 2006*

III. Market Competition

3.1 Domestic Competition

China itself is a large producer of a wide range of food commodities, from grain, oilseeds, fruit to meat, poultry and aquatic products. (See *Table 3.1 for the output of main food commodities in China.*) CY 2007 recorded moderate growth in the output of most agricultural products in China, with exception of pork and rapeseeds.

The need to import food products still exists, given the gap between the comparatively short domestic production, great domestic demand and surging food prices resulting from rising incomes and living standards, population growth, shrinking arable land, recent catastrophic disasters and trade liberalization.

To meet domestic demand, China imports in large volume a wide range of food products, including grain and cereal, oilseeds, fruit and nuts, meat, poultry products, seafood, and dairy products. Surging domestic food and feed prices, reduced production of pork, and constant demand of good quality food by the growing middle and upper class, altogether reinforce the need for imports of certain food products. To secure the supply for domestic demand, the Chinese government has recently initiated a series of actions to restrict exports and encourage imports.

Grain

Overall consumption of grains is slightly declining as consumers shift from carbohydrates to more protein in their diet. However, demand for high quality grains, including wheat and rice, is moderately increasing, as wealthy consumers favor diverse high quality food products such as baked goods, biscuits and noodles. China, as the largest brewer in the world, has to import substantial barley to back inadequate domestic production. The country retains a long term self-sufficiency strategy for food grain, e.g., wheat, rice and corn. To ease inflationary pressures and secure the domestic supply, the government has tightened its control on grain export. Globally surging prices of wheat and rice make the imported commodities less competitive than those domestic ones.

Oilseeds

Total oilseeds production in China grows slightly due to increased plantings in response to the record high oilseed prices and government supported programs. Use of Chinese oilseeds, particularly soybean, for food has been increasing because of growing demand for cooking oil, soy protein and soy food products. Opportunities arise for imports of edible oil or oil-bearing crops to satisfy rising demand. Imports in large volume of soybeans and edible oil in recent years reflect such demand.

Poultry

Poultry meat production in China continued to grow 12 percent to an estimated 11.5 million tons in CY2007. High pork prices have boosted sales of poultry meat as consumers substitute expensive pork with poultry. Increasing expatriate population and the popular western cuisine have also dramatically beefed up the import of turkey, a non-traditional poultry product into China.

Meat

China's meat production in CY 2007 and 2008 has been badly hit by higher input prices, epidemic swine disease, heavy snowstorm in the past winter, and the recent catastrophic

earthquakes in Sichuan provinces. Despite the slight growth of beef production, FAS Beijing estimated that China will increase its beef imports by four fold to 30,000 MT in 2008 to meet the strong domestic demand¹.

Pork production in China is slowly recovering from the deep decline in 2007 caused by blue ear disease. The recent magnitude earthquake in Sichuan where reportedly 4-5 million heads of swine were immediately affected by the earthquake will place tension on the country's rebounding production and in turn on pork prices in the coming months. Imports of pork remain strong, as a way to supply the strong domestic market and ease the pressure of surging prices that challenges the Chinese government.

Aquatic products

Both the growing domestic demand and strong export markets drive the growth of China's aquatic production at a slow rate. About two-thirds of China's aquatic production come from both seawater and freshwater farms, and the remainder comes from aquatic catch. Domestic products hold increasing market share due to improved quality, available supply and competitive prices. China is also a large seafood processor, with most processed products for re-export. It is the largest recipient of the U.S. seafood export while the US is the second largest recipient of the processed seafood products from China. Potential for aquatic imports for domestic consumption lays in the high-end niche as well as the mass market which requires consistent supply at reasonable prices.

Dairy Products

To improve public nutrition, Chinese government furthers aggressive encouragement of milk consumption and domestic milk production. Domestic milk production grows exponentially along with the rising total milk consumption. However, per capita milk consumption is low, due to the country's large population and low starting point. The latest food pagoda launched in January 2008 (equivalent to the U.S. food pyramid) triples the recommendation of dairy products for individuals over 6 years old to a daily intake of 0.66 lbs (By comparison, the U.S. food pyramid recommends 1-1.5 lbs a day.). Despite continuously growing milk production in China, in the next 5-10 years, China will still need imports of dairy products, e.g., powdered milk, cheese and whey, to meet its growing demand.

¹ GAIN CH8014 *Livestock and Products Semi Annual*, J. Zhang and E. Trachtenberg.

Table 3.1 Domestic Agricultural Output in China, Yield of Farm Crops

(10,000 tons)	2002	2003	2004	2005	2006*	Growth % (2006/2005)
Grain	45,705.8	43,069.5	46,946.9	48,402.2	49,747.9	2.8
Cereal	39,798.7	37,428.7	41,157.2	42,776.0	44,237.3	3.4
Rice	17,453.9	16,065.6	17,908.8	18,058.8	18,257.2	1.1
Wheat	9,029.0	8,648.8	9,195.2	9,744.5	10,446.7	7.2
Corn	12,130.8	11,583.0	13,028.7	13,936.5	14,548.2	4.4
Oil-bearing Crops	2,897.2	2,811.0	3,065.9	3,077.1	3,059.4	-0.6
Peanuts	1,481.8	1,342.0	1,434.2	1,434.2	1,466.6	2.3
Rapeseeds	1,055.2	1,142.0	1,318.2	1,305.2	1,264.9	-3.1
Sesame	89.5	59.3	70.4	62.5	66.5	6.4
Fruits	6,952.0	14,517.4	15,340.9	16,120.1	17,239.9	6.9
Apples	1,924.1	2,110.2	2,367.5	2,401.1	2,605.9	8.5
Grapes	447.9	517.6	567.5	579.4	627.1	8.2
Citrus	1,199.0	1,345.4	1,495.8	1,591.9	1,789.8	12.4
Meat	6,586.5	6,932.9	7,244.8	7,743.1	8,051.4	4.0
Pork	4,326.6	4,518.6	4,701.6	5,010.6	5,197.2	3.7
Beef	584.6	630.4	675.9	711.5	750.0	5.4
Mutton	316.7	357.2	399.3	435.5	469.7	7.9
Milk	1,400.4	1,848.6	2,368.4	2,864.8	3,302.5	15.3
Poultry Eggs	2,462.7	2,606.7	2,723.7	2,879.5	2,945.6	2.3
Aquatic Products	4,564.5	4,704.6	4,901.8	5,107.6	5,290.4	3.6
Seawater Products	2,646.3	2,685.8	2,767.8	2,838.3	2,887.7	1.7
Freshwater Products	1,918.2	2,018.8	2,134.0	2,269.3	2,402.7	5.9

*Latest available full year data

Source: *China Statistical Yearbooks, 2003-2007*

3.2 Competition of Imports - 2007

Data in Section 3.2 are sourced from China Customs statistics of imports in CY2007 retrieved by *Global Trade Atlas System*. Commodities are categorized by respective HS codes.

3.2.1 Soybeans (HS Code: 1201)

	Imports into China (CY 2007)	Y/Y Growth (%)	U.S. Share (%)
1201 Soybeans			
Value (1,000,000 US\$)			
from all countries	11,465.0	53.1	-----
from the US	4,251.3	56.3	37.1
Volume (1,000 MT)			
from all countries	30,818.3	9.0	-----
from the US	11,634.5	17.7	37.8

Highlight of Main Products

- Due to strong domestic demand, China's soybean imports reached record highs in CY 2007.
- Skyrocketing prices pushed the import value up 53 percent, despite only a 9 percent increase in volume.
- All soybeans imported to China were yellow soya beans (120100).
- Though most of the imported soybeans are used for oil crushing and feed use, interest in food use is increasing.

Key Exporting Countries

- The US, Brazil and Argentina are the largest soybean suppliers to China.
- The US overtook Brazil in CY 2007 as the largest soybean exporter to China, holding a 37.8 percent market share in volume terms.
- Brazil and Argentina closely followed the US, respectively holding a share of 34.3 and 26.6 percent in volume.

Main Importing Ports and Share (% in volume terms)

Soybean imports entering China through various ports across the country:

- North China: Qingdao (19.7), Shijiazhuang (5.2), Tianjin (4.4), Dalian (3.8) and Zhengzhou (1.7)
- South China: Huangpu (10.0), Nanning (8.3), Xiamen (4.7), Zhanjiang (3.5), Shenzhen (3.3), Fuzhou (2.3) and Jiangmen (1.9)
- East China: Nanjing (20.6), Hangzhou (4.2) and Ningbo (4.0)

3.2.2 Fish and Seafood (HS Code: 03)

	Imports into China (CY 2007)	Y/Y Growth (%)	U.S. Share (%)
03 Fish and Seafood			
Value (million US\$)			
from all countries	3,443.0	9.0	-----
from the US	461.8	13.6	13.4
Volume (1,000 MT)			
from all countries	2,319.3	6.5	-----
from the US	N/A	N/A	N/A

Highlight of Main Products

- Frozen fish (0303), including cod, salmon, plaice, valued at US\$ 2.6 billion, accounting for 76.5 percent of the total seafood import value.
- Other seafood (0307), mostly cuttle fish, squid and sea snails, valued at US\$ 386.8 million, a 11.2 percent share of the total seafood imports.
- Crustaceans (0306), valued at US\$ 299.9 million, holding a 8.7 percent share of seafood imports.

Key Exporting Countries

Most of China's seafood and fish imports is processed for re-export. A large number of countries exports to China, with Russia and the US lead in the group.

- Russia remained the largest seafood exporter to China, holding a 38.8 percent share in value.
- The US as the second largest exporter, held a 13.4 percent share.
- South Korea, Canada, Norway and Japan respectively shared 4-6 percent of the market.
- The rest of the market is shared by many countries who each only hold a fraction share.

Main Importing Ports and Share (% in value terms)

Most seafood is imported into China via Qingdao (58%) and Dalian (23%) for re-export processing. Shanghai ranks third, handling a small share (4.6%).

3.2.3 Meat (HS Code: 02)

	Imports into China (CY 2007)	Y/Y Growth (%)	U.S. Share (%)
02 Meat			
Value (million US\$)			
from all countries	1,519.1	121.4	-----
from the US	764.3	113.7	50.3
Volume (1,000 MT)			
from all countries	1,340.3	57.6	-----
from the US	657.7	40.7	49.1

Highlight of Main Products

In CY 2007, short pork supply and the resulting high prices in China beefed up imports of all poultry and meat products. A large volume of pork was also imported to offset the shortage and high prices of pork in China. The strong growth was also recorded in the imports of beef (258 percent in volume) and edible animal offal (98 percent in volume).

- **Poultry products (0207)** mostly chicken paws, wing tips, leg quarters and drum sticks, accounted for 62.2 percent in value of China's total imports of meat products. Imports of poultry products in CY 2007 significantly increased 36.6 percent in volume term or 104.2 percent in value term. Sales of U.S. poultry products doubled the previous year, mainly owing to high prices and tight supply, together with high pork prices in China, owing to Blue Ear disease which surfaced last April and decimated swine populations.

- **Animal offal (0206)**, accounted for 30 percent of the meat import volume in CY 2007, up 98 percent from the year before.

- **Pork (0203)**, accounting for 6.3 percent of the total meat import volume in CY 2007, increased 260 percent from the previous year.

- **Lamb (0204)**, increased only 26.5 percent in volume, the lowest growth in the meat category.

- **Beef (0202 and 0201)**, sharing a fraction of China's meat imports, recorded a 258 percent increase in CY 2007 from the previous year. Australia is the top exporter holding more than 50 percent of the import market. When the China market will be reopened to the U.S. beef remains unknown.

Key Exporting Countries

- US, as the largest meat exporter to China, held almost 50 percent of China's meat import in volume.

- The rest of the market is shared by France (sharing a 15.5 percent volume of China's meat imports), Brazil (12.2%), Argentina (7.6%), Denmark (6.3%), Canada (4.1%), New Zealand (2.3%) and Australia (1.7%).

Main Importing Ports and Share (% in volume terms)

About two-thirds of China's meat imports enter into the country via South China, mostly Guangzhou and Shenzhen. Shanghai handled 17.8 percent of China's meat imports in CY 2007. Meanwhile, Dalian, and Tianjin are the largest ports of entry for meat products in northern China, respectively handling 8.9 and 4.3 percent of the country's import volume.

3.2.4 Edible Fruit and Nuts (HS Code: 08)

	Imports into China (CY 2007)	Y/Y Growth (%)	U.S. Share (%)
08 Edible Fruit and Nuts			
Value (million US\$)			
from all countries	912.4	23.7	-----
from the US	114.2	1.5	12.5
Volume (1,000 MT)			
from all countries	1,394.0	5.6	-----
from the US	88.4	-17.5	6.3

Highlight of Main Products

This category is highly fragmented, as China imports a wide range of fruit and nuts from various countries:

Other nuts, including almonds, hazelnuts, pistachios etc.	(0802)	US\$ 127.6 million
Bananas, plantains	(0803)	US\$ 110.6 million
Grapes and raisin	(0806)	US\$ 81.0 million
Frozen fruit and nuts, including strawberry, raspberry, blackberry, etc.	(0811)	US\$ 78.3 million
Date, fig, pineapple, etc.	(0804)	US\$ 70.4 million
Other dried fruit, including dried longan and plums	(0813)	US\$ 60.3 million
Citrus, fresh or dried	(0805)	US\$ 54.8 million
Coco, Brazil nuts, Cashew nuts	(0801)	US\$ 32.5 million

Key Exporting Countries

The competition in China is fierce, as many countries export to this market.

- Thailand is the largest exporter of fruit and nuts to China, accounting for 27.5 percent of the value of China's imports of this category in CY 2007.
- The US is the second largest exporter to China in this category, holding a 12.5 percent share in CY 2007.
- Vietnam and Philippines held a similar share as the US in CY 2007, respectively 12.3 and 12.1 percent.
- Chile held a 7.1 percent share in CY 2007, followed by Russia, New Zealand, Iran, Sweden, South Korea, Indonesia, Finland, Peru, Australia and Canada, respectively sharing a 1-4 percent cut.
- The US, Russia, Iran and South Korea are the main nuts exporters to China, while Thailand, the US, Philippines, Vietnam, Chile, New Zealand, Australia and South Africa are the main exporters of fruit.

Main Importing Ports and Share (% in volume terms)

- South China handles about two-thirds of China's imports of fruit and nuts. Key importing ports in this region include Nanning (23.6%), Guangzhou (18.5%), Haikou (7.6%) and Shenzhen (7.2%).
- Dalian in north China and Shanghai in east China are the largest ports of entry out of southern China, respectively handling 13.6 and 12.7 of the country's import volume in CY2007.

3.2.5 Dairy Products (HS Code: 04)

	Imports into China (CY 2007)	Y/Y Growth (%)	U.S. Share (%)
04 Dairy Products			
Value (million US\$)			
from all countries	744.6	33.4	-----
from the US	106.8	26.4	14.3
Volume (1,000 MT)			
from all countries	298.7	14.0	-----
from the US	N/A	N/A	N/A

Highlight of Main Products

China's imports of dairy products are mostly powdered milk and whey. Cheese and butter only accounts for a fraction. Global high prices and short supply lowered the import volume of powdered milk and whey in CY2007, though import value increased significantly.

- Powdered milk (0402)

Imports fell 27.2 percent to 99,000 tons in CY 2007, due to global high prices and short supply. New Zealand was the largest exporter, holding a 72.6 percent of China's import volume. The rest were shared by Australia (12.6%), the US (6.6%), France (1.8%) and other countries.

- Whey (0404)

Import volume dropped 9.2 percent to 168,000 tons in CY 2007, due to global high prices and short supply. The US as the largest exporter, held a 29.7 percent of China's import volume in CY 2007. France closely followed with a 28.1 percent share. New Zealand, Argentina, Ireland, Australia, Germany, the Netherlands and Finland respectively had a 2.9-7.3 percent share.

- Cheese and butter (0405 and 0406)

Thanks to the fast growing HRI and bakery sectors in China, cheese and butter gradually gain popularity in large cities from a small base. Imports of cheese increased 33.3 percent to 13,200 MT in CY 2007, while the imports of butter grew 9.6 percent to 14,000 MT. New Zealand and Australia are the largest exporters, while the US and European countries hold a fraction in the market.

Main Importing Ports and Share (% in volume terms)

East China: Shanghai (34.8%) and Nanjing (1.8%)

North China: Tianjin (31.8%), Dalian (4.7%), Beijing (4.2%) and Qingdao (4.2%)

South China: Huangpu (7.0%), Gongbei (4.7%) and Guangzhou (1.9%)

3.2.6 Preserved Food (HS Code: 20)

	Imports into China (CY 2007)	Y/Y Growth (%)	U.S. Share (%)
20 Preserved Food			
Value (million US\$)			
from all countries	272.9	37.6	-----
from the US	79.3	30.6	29.1
Volume (1,000 MT)			
from all countries	201.3	9.1	-----
from the US	74.9	11.5	37.2

Highlight of Main Products

- **Fruit juice (2009)** imports in CY 2007 grew 47.7 percent in value to US\$ 146 million, despite only a 6.8 percent increase in volume. Main exporting countries are Brazil and Israel, respectively holding 50.3 and 24.5 percent share of the volume in CY 2007. US ranked third with a 4.4 percent share.
- **Prepared fruit (2008)** Import value grew 30 percent to US\$ 57 million in CY 2007. Prepared citrus from the US and Brazil accounted for the majority.
- **Prepared potato (2004)** Import value increased by 22 percent to US\$ 54 million in CY 2007, despite a 3 percent drop in volume. Most imports were from the US (73 percent of the volume), followed by Canada with 22.3 percent share in volume.

Main Importing Ports and Share (% in volume term)

- Shanghai is the largest importing port in China for preserved food products, accounting for 45 percent of the volume.
- South China: Shenzhen (13.7), Huangpu (5.5), Xiamen (2.7) and Guangzhou (1.3)
- North China: Tianjin (13.0), Beijing (7.3), Qingdao (4.7) and Dalian (2.1)

3.2.7 Cereal (HS Code: 10)

	Imports into China (CY 2007)	Y/Y Growth (%)	U.S. Share (%)
10 Cereal			
Value (million US\$)			
from all countries	515.0	-37.3	-----
from the US	6.2	-85.7	1.2
Volume (1,000 MT)			
from all countries	1,520.5	-57.2	-----
from the US	20.0	-91.9	1.3

Highlight of Main Products

China's imports of cereal in 2007 dramatically dropped in CY 2007, due to the globally record high prices. Barley (1003), rice (1006) and wheat (1001) consist of the majority of the cereal imports.

- Barley (1003)

Barley imports dropped 57.5 percent in volume to 913,400 MT in CY 2007, at a value of US\$ 266.8 million. Barley is in great demand in China which has become the largest brewery in the world. Majority of the imports was from Australia (54.2% of import value in CY 2007), Canada (36.4%) and France (9.4%).

- Rice (1006)

China's rice imports in CY 2007 reduced 34.4 percent in volume to 471,500 MT, while import value dropped 24.6 percent to US\$ 217.5 million. Thailand is the largest rice exporter to China, accounting for 93 percent of China's rice imports. Vietnam as the second largest exporter held only 5.6 percent share in CY 2007. About 90 percent of the imported rice was sold to South China, especially Guangdong province for local consumption.

- Wheat (1001)

China dramatically reduced its wheat imports in CY 2007 due to global high prices. Wheat imports to China dropped 85.7 percent from a year ago to 83,400 MT, mostly durum. All the wheat imports entered to Guangdong province for milling via Shenzhen, Huangpu and Guangzhou.

- Corn (1005)

High prices pushed China's corn imports down 46 percent to 35,200 MT in CY 2007. Laos, Myanmar and the US were the leading exporters, respectively holding a share of 30.9, 24 and 21.2 percent in CY 2007.

- Oats (1004)

Oat imports into China dropped 67.8 percent to 5,218 MT in CY 2007. Australia was the monopoly foreign supplier in CY 2007, with all imports entering South China via Shenzhen, Nanning and Huangpu.

3.2.8 Fats and Oils (HS Code: 15)

	Imports into China (CY 2007)	Y/Y Growth (%)	U.S. Share (%)
15 Fats and Oils			
Value (million US\$)			
from all countries	7,576.4	93.1	-----
from the US	135.0	408.3	1.8
Volume (1,000 MT)			
from all countries	10,203.0	24.9	-----
from the US	176.6	428.8	1.7

Highlight of Main Products

Despite global high prices, China's imports of oils and fats were dramatically boosted by high prices and strong demand in the domestic market. Most of the imports are:

	HS Code	Value (million US\$)
Palm oil	(1511)	3,684.8
Soybean oil	(1507)	2,145.5
Coconut, palm kernels or Babassu oil	(1513)	403.7
Rapeseed, colzo or mustard oil	(1514)	305.1
Animal and vegetable oil and fats, hydrogenated	(1516)	297.4
Bovine, sheep, goat fat	(1502)	243.9
Margarine	(1517)	198.8
Other fixed vegetable oils and fats	(1515)	103.6
Various seed oil	(1512)	49.3
Olive oil	(1509)	32.0
Fats and oils - fish & marine mammal	(1504)	31.3
Peanut oil, no chemical modified	(1508)	14.0

Key Exporting Countries

Malaysia, Argentina and Indonesia were the largest oil exporter to China, respectively holding 38.3, 23.2 and 21.1 percent of the import value in CY 2007. The rest of the market was fragmented by a number of countries, including Brazil, Canada, Australia and the United States.

Main Importing Ports and Share (% in volume term)

East China: Nanjing (30.7%), Shanghai (7.5%) and Hangzhou (2.8%)

North China: Tianjin (19.8%) and Qingdao (4.0%)

South China: Huangpu (17.0%), Shenzhen (4.9%), Xiamen (2.7%) and Nanning (2.2%)

3.2.9 Vegetables (HS Code: 07)

	Imports into China (CY 2007)	Y/Y Growth (%)	U.S. Share (%)
07 Vegetables			
Value (million US\$)			
from all countries	801.2	6.0	-----
from the US	24.5	-0.2	3.1
Volume (1,000 MT)			
from all countries	4,974.0	7.4	-----
from the US	32.8	-29.9	0.7

Highlight of Main Products

- **Cassava and arrowroot (0714)**, import value up 6.5 percent to US\$ 661 million in CY2007, accounting for 82.5% of the total vegetable imports. Most of the imports was from Thailand (69%) and Vietnam (27.2%).
- **Dried peas (0713)**, import value up 10 percent to US\$ 108.7 million in CY 2007. Canada was the largest supplier holding 58.1 percent share, followed by India (24.3%), Myanmar (10.9%) and the US (2.9%).
- **Frozen vegetables (0710)**, imports up 3.8 percent to US\$ 20.7 million, accounting for 3.8 percent of the total vegetable imports. U.S. dominates this category, supplying 93.7 percent of the total imports of frozen vegetable in CY 2007. Most of the imports entered to the eastern and northern China via Shanghai (41.8% of import value), Qingdao (21.1%), Ningbo (12.7%), Beijing (7.5%) and Dalian (4.1%). Only a small percent of the imports entered to South China, via Huangpu (6.7%) and Xiamen (4.7%).

3.2.10 Preparations of Flour (HS Code: 1901)

	Imports into China (CY 2007)	Y/Y Growth (%)	U.S. Share (%)
<u>1901 Preparations of Flour</u>			
Value (million US\$)			
from all countries	355.0	26.0	-----
from the US	12.7	0.6	3.6
Volume (1,000 MT)			
from all countries	75.0	8.6	-----
from the US	6.0	-13.5	7.9

Highlight of Main Products

Fast growing baking industry in China boosts imports of flour preparations. In CY 2007, most of the imports entered to China via Shanghai (55.8% of the import value) in eastern China, Shenzhen (28.1%) and Huangpu (7.6%) in southern China.

Key Exporting Countries

Many countries aggressively promote their products to the baking industry in China, including Singapore (accounting for 36.6% of the import value), New Zealand (20.9%), Denmark (11.7%), Ireland (8.2%), the Netherlands (7.6%), Australia (5.2%) and the US (3.6%).

IV. Best Product Prospects

Best product prospects are:

- Soybeans
- Seafood
- Poultry products
- Beef
- Dried Fruit & Nuts
- Fresh Fruit
- High Value Dairy Products
- Grains & Cereal
- Potato Products
- Baking Ingredients
- Food Additives

Please refer to Appendix 3 at the end of this report for further details.

V. Further Reference

CH7403	03/16/2007	Emerging City Markets: The Next Economic Miracle
CH7071	09/21/2007	Tree Nuts Annual 2007
CH7081	10/30/2007	Dried Fruit Annual 2007
CH7609	05/16/2007	Bustling Ports in South China
CH7610	06/08/2007	South China, Vibrant Gateway for China's Imported Fruit
CH7624	10/24/2007	Moon Cake Mania-Golden Opportunities for Chinese Baking Sector, But What about U.S. Ingredients?
CH8025	04/21/2008	Increasing Food Prices
CH8603	05/14/2008	South China's Thirst for U.S. Fruit and Vegetable Juice Keeps Growing
CH8605	05/30/2008	South China, Where Opportunity Knocks for High Value U.S. Dairy Ingredients
CH8904	06/03/2008	Sichuan Earthquake Shakes Up Local Agriculture

VI. Post Contact Information

For further information about the China market, please visit our website at www.usdachina.org or contact any of the following USDA offices in China:

FAS/Office of Agricultural Affairs (OAA), Beijing

5-2 Qijiyuan Diplomatic Compound
Jianguomenwai, Beijing, China, 100600
Ph: (8610) 6532-1953
Fax: (8610) 6532-2962
E-mail: agbeijing@fas.usda.gov

Agricultural Trade Office (ATO), Beijing

Kerry Center, South Tower
24th Floor Suite #2425
No. 1 Guanghua Lu, Beijing, China 100020
Ph: (8610) 8529-6418
Fx: (8610) 8529-6692
E-mail: atobeijing@fas.usda.gov

IPR Office

E-mail: yuanchuan.liang@usda.gov

Agricultural Trade Office (ATO), Guangzhou

14/F, Office Tower
China Hotel, Guangzhou, China 510015
Ph: (86-20) 8667-7553
Fx: (86-20) 8666-0703
E-mail: atoguangzhou@fas.usda.gov

Agricultural Trade Office (ATO), Shanghai

Shanghai Center, Suite 331
1376 Nanjing West Road, Shanghai, China 200040
Ph: (8621) 6279-8622
Fx: (8621) 6279-8336
E-mail: atoshanghai@fas.usda.gov

Agricultural Trade Office (ATO), Chengdu

1222 Western Tower
No. 19, 4th Section, Renmin Nan Road, Chengdu, China 610041
Ph: (8628) 8526 8668
Fx: (8628) 8526 8118
E-mail: atochengdu@fas.usda.gov

Animal and Plant Health Inspection Service (APHIS), Beijing

Room 618, Beijing International Club Office Building
No. 21 Jianguomenwai Avenue, Beijing, China 100020
Ph: (8610) 6532-3212
Fx: (8610) 6532-5813
E-mail: theresa.boyle@aphis.usda.gov

Appendix 1. Distribution Channel Members

Traders / Importers

Traders, often importers, are self-financed, specialized business organizations or people who have their own sales and distribution network. They can purchase large quantities of goods directly from manufacturers / exporters or from another importing company. Imported goods are sold directly or through an agent to the food processors / manufacturers with transfer of assets. Some importers are also processors who own processing and packing facilities. To a large extent, traders control the demand and the pricing of the goods to the clients.

Logistics Providers

There are many international logistics providers in ports and free trade zones offering shipping, domestic transportation, customs clearance, warehousing services.

Customs Clearance Agent

Contracted by importers or logistics provider to handle customs clearance and import inspection issues with service charge applied.

Direct Distribution

Manufacturers / exporters set up sales outlet and sell products directly in China rather than through a local business organization or person. The advantage is that the manufacturers / exporters can meet consumers face-to-face to learn about market conditions and trends. They can also reap the benefits of their sales promptly. The drawback is the need to invest in developing a sales network and the high cost of learning how to operate in a foreign market. This method should be made easier with China's revamping of the import-export system.

Gray Channel

The Gray Channel refers to the distribution connection transferring shipments via Hong Kong to China without going through the official import channel of customs and import inspection. This channel has historically been cheaper than official channels as imported goods are often shipped from Hong Kong outside of official channels to evade import duty and VAT payments. U.S. exporters should know that this channel is illegal and discouraged. Goods traded via the gray channel is risky, due to lack of reliable technical expertise provided by gray channel operators and the authority's anti-smuggling enforcement. Non-U.S. products may deliberately "mislabelled" as U.S. products in the gray channel. Resulting from the lowered import tariff, the gap between legal channel and gray channel costs is narrowing, and fewer goods enter South China illegally.

(Source: GAIN CH7604 Food Processing 2007)

Appendix 2. Import Documentation

Exporters must complete the following documentation:

- ❖ Bill of Lading
- ❖ Label Certificate (required for all packaged food products)
- ❖ Invoice
- ❖ Packing list describing item, weight, and packing material
- ❖ Certificate of Origin
- ❖ Sanitary / Phytosanitary Certificates
- ❖ Packing Declaration Form (for packing without wood material)
- ❖ Fumigation Inspection Certificate (for packing with wood material)

Importers are responsible for the following documentation:

- ❖ Import authorization document
- ❖ Customs declaration documents
- ❖ Quarantine Certificates
- ❖ Additional product specific documents

(Source: GAIN CH7604 Food Processing 2007)

Appendix 3. Good Prospects for Ingredients in China

Soybeans

China does not have enough supply to meet increasing domestic demand for soybeans. Shortfalls of domestic oil-bearing seeds for years has resulted in greater demand for soybean imported from other countries. In 2006, China's import of soybeans exceeded 28 million tons at a 6.3 percent rise from the previous year. Meanwhile, soybean exports dropped to only 395,000 tons by 4.5 percent, a much lower level compared to the import volume. The productions of high-value product such as soybean protein, as well as increasing proportion of soybeans in the daily diet also boost demand. The US is one of the largest soybean exporter to China, enjoying 34 percent of the market share. The market is in favor for the US to further extend market share in China.

Seafood

China's national statistics show a significant increase of seafood in Chinese's daily diet, especially in the more affluent region. The well developed restaurant sector, especially upscale restaurants, wants for top-quality food ingredients to better serve discriminating tastes. Urban dwellers in big cities, especially South China which offers diverse food options, are crazy about premier seafood. A significant portion of China's seafood import is consumed by processing plants for re-export. High quality and uniqueness originating from the growing area can place U.S. seafood at a very competitive position in the China market. Local demand for high quality seafood in affluent regions gives rise to promising prospects for high quality U.S. seafood such as Alaska seafood.

Poultry products

The US and China fit very well in the poultry consumption, as both have large consumption, but on totally different parts of a chicken. Chinese love chicken paws, wings or wing tips, and Americans favor the meaty chicken breast. For years, China has been the largest importer of U.S. poultry products. In addition, per capita consumption of poultry, especially in urban area, is also increasing. The demand for U.S. poultry is very likely to continue and increase, as more Chinese consumers, especially those in a less developed region, with the increasing disposable income, are likely to purchase larger quantity of such affordable food items as chicken paws and wing-tips.

Beef

Similarly to seafood, good prospects for beef originate from Chinese consumers' pursuit of premier food. China remains closed to U.S. beef, but demand will be immediate once the market is resumed, as upscale restaurants and hotels all recognize the superior taste and quality of U.S. beef. It is advisable for potential exporters to keep a close eye on the China market.

Dried Fruit & Nuts

The versatility of U.S. dried fruit and nuts has a lot to offer affluent Chinese consumers. The pursuit of leisure, health, convenience in life has created huge demand for food in various forms, e.g., snacks, baked products, convenience food etc, into which U.S. dried fruit and nuts can certainly add value. Furthermore, Chinese has a traditional belief that some types of food possess specific health attributes. Such belief with the increasing disposable income has led many to a higher level of consumption of pricey food items believed to possess certain health benefit. Many of the U.S. dried fruit and nuts, have been scientifically proved to contain high levels of certain types of healthy substances, for example, rich anti-oxidants in blueberry, high vitamin E content in almond, etc. Educating consumers will certainly differentiate the product and encourage the consumption.

Fresh Fruit

U.S. fruit is popular in China despite higher prices compared to domestic fruit in season. In addition to consumption for the home, consumers buy pricey, usually imported fruit as gift to give important personal or business contacts which has become popular practice, especially on such occasions as important festivals, or visiting friends. In spite of relatively high prices, consistent high quality and uniqueness of U.S. fruits are strong attributes to affluent Chinese consumers in the highly competitive market. *(Refer to GAIN CH 7610 for more details)*

High Value Dairy Products

The high-value dairy market has very limited presence in China market, despite the fact that milk consumption has skyrocketed in recent years. Dairy products, especially high value dairy products, such as cheese, has very limited presence in the traditional Chinese diet, and as a result, consumers have little knowledge of these products. However, there is promising potential for high value dairy products to fit food consumption pattern that is becoming more diverse and richer in protein, especially in well-developed areas. Food containing dairy ingredients, e.g. cheesecake, has started to gain popularity in the big cities. Increasing number of baked products is entering the food market in China. The fast growing sectors of bakery and health food manufacturing deliver high value dairy products to consumers. Increasing potential consumer's awareness and knowledge of dairy products ignite the demand for high value dairy products by a larger consumer group. *(Refer to GAIN CH8605 for more details)*

Grain & Cereal

Fast growing food processing sectors and consumers' changing life style in well-developed areas has provided sound opportunities for high quality grain and cereal ingredients such as wheat and oats. Food sectors, e.g., bakery need high quality wheat flour to enhance the their product quality in terms of texture, content of nutritional substance and taste. In addition, consumers in well-developed areas favor baked products and ready-to-eat cereals, especially for breakfast, which simultaneously offer health benefit and convenience. Opportunities for high quality grain and cereal ingredients may also arise in developed area in China where per capita consumption of grain has started to decline, as health conscious consumers are willing to include less carbohydrates, but more nutritional dietary fiber and protein which are richer in U.S. grain and cereal.

Potato Products

Despite being the largest potato grower in the world, China annually imports processed potato products worth multimillions. Processed potato products, for example, dehydrated potato, has the versatility to be used as ingredients in food manufacturing, cooking, and baking.

Baking Ingredients

Such products are well suited to the fast growing baking sectors which attempt to differentiate their products against competitors.

Food Additives

Additives that enhance the features of processed products, such as preservatives, emulsifiers, flavorings or colorings, are in good demand, especially for large or upscale enterprises.

(Source: GAIN CH7604 Food Processing 2007)