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Global Agricultural Information Network

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Report Highlights:

Fluid milk imports into China will continue to grow in 2017 due to the diminished size of China's dairy herd and continued low milk prices in the European Union (EU) and New Zealand. Post forecasts 2017 fluid milk imports at 900,000 metric tons—a 38 percent increase over 2016. Despite the high favorability ratings of U.S.-origin food products among Chinese consumers, U.S. dairy imports are still hindered by China's recent registration requirements.

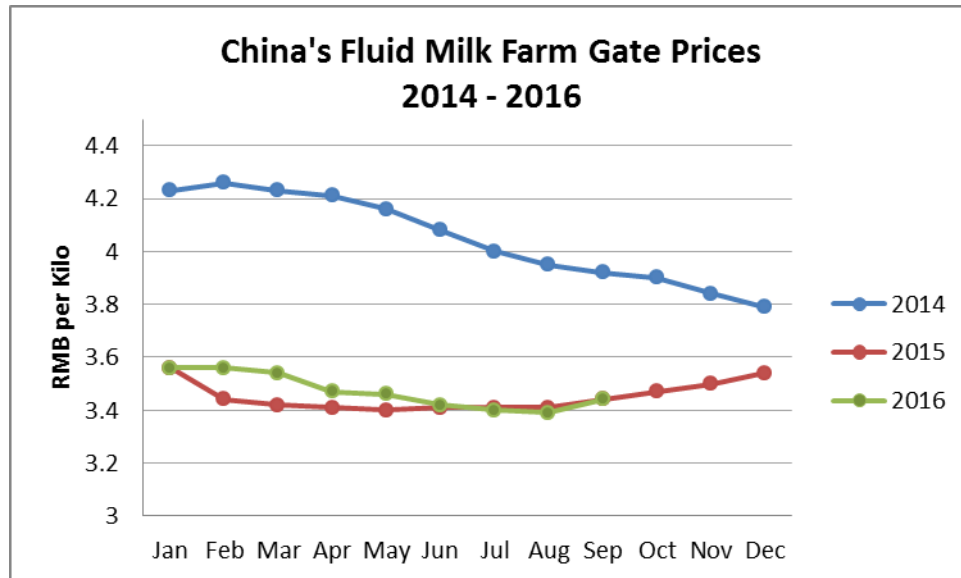
Fluid milk PS&D table

Dairy, Milk, Fluid Market Begin Year	2015		2016		2017	
	Jan 2015		Jan 2016		Jan 2017	
	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post
China						
Cows In Milk*	8400	8400	8500	8000	-	7000
Cows Milk Production	37550	37550	38000	35700	-	35000
Other Milk Production	1500	1500	1450	1600	-	1500
Total Production	39050	39050	39450	37300	-	36500
Other Imports	460	460	650	650	-	900
Total Imports	460	460	650	650	-	900
Total Supply	39510	39510	40100	37950	-	37400
Other Exports	25	25	25	20	-	20
Total Exports	25	25	25	20	-	20
Fluid Use Dom. Consum.	15360	15360	15570	14600	-	15380
Factory Use Consum.	24125	24125	24505	23330	-	22000
Feed Use Dom. Consum.	0	0	0	0	-	0
Total Dom. Consumption	39485	39485	40075	37930	-	37380
Total Distribution	39510	39510	40100	37950	-	37400
(*Measured in 1,000 head. All other figures measured in 1,000 MT.)						

Production

Milk production will remain flat in 2017

Post forecasts China's 2017 milk production at 35 million tons, basically unchanged from 2016's production figures, due to low-priced imports, stable domestic consumption patterns, and whole milk powder (WMP) substitution. Post also adjusted 2016's production estimate down to 35.7 million tons, a 5 percent decrease from 2015. Low domestic and international milk prices were the cause for this production reduction.



Source: China's Ministry of Agriculture

Low prices continue to depress Chinese production. Over half of China's dairy farms operated at a loss in 2016. It is estimated that 60 to 70 percent of fluid milk production in China comes from large scale dairy farms, while middle to small dairy farms occupy the remaining 30 to 40 percent. In 2016, many small dairy farms closed up shop and several large dairy operations culled their herds. Post estimates that China's entire dairy cattle herd was reduced by 10 percent in 2016. In further efforts to slow production, many Chinese dairy farms altered their feed frequency and/or formulation.

As a result of the herd reduction in 2016, Post forecasts that the herd size will not fully recover in 2017, causing fluid milk production to remain flat or possibly decrease slightly to 35 million tons. If the milk price recovers sufficiently in 2017, the production numbers may be raised slightly, but stagnant demand for domestically produced fluid milk will likely forestall a significant increase in production. Not only is domestic demand flat, but international prices are expected to remain low, especially in the European Union and New Zealand which together occupy 97 percent of Chinese fluid milk imports.

A further constraint on increased production is the widespread use of reconstituted whole milk powder (WMP). China is one of the only countries that reconstitutes WMP back into fluid milk for retail sale. As long as the imported WMP price is significantly cheaper than the domestic fluid milk price, dairy processors will continue to use WMP to produce milk and other dairy products, further curbing demand for increased fluid milk production.

Consumption

Fluid milk consumption demand will be stagnant, with a 1 or 2-percent increase at most.

As China's economic slowdown continues, Post forecasts milk consumption will remain flat, with a possible increase of 1 or 2 percent, driven by continued population growth and urbanization. Chinese consumers' milk consumption is still very low by international standards—about 33kg per capita, or less than one third of the world average. Milk consumption has plenty of growth potential but food safety concerns drag on increased consumer demand.

To analyze the fluid milk consumption in China, both imported fluid milk and reconstituted WMP must be considered. Chinese consumers generally prefer imported milk over domestic milk due to perceived differences in safety and quality. In addition, dairy processors prefer the higher profit margins associated with imported milk and higher-end products. The cheap plastic bag milk which only costs about USD 0.15 per bag have been abandoned by most dairy processors in favor of high-end products. As a result, these high-end products are dominating the market and alienating price-driven consumers, especially in rural areas, forcing them to substitute cheaper protein sources like soy products.

Trade

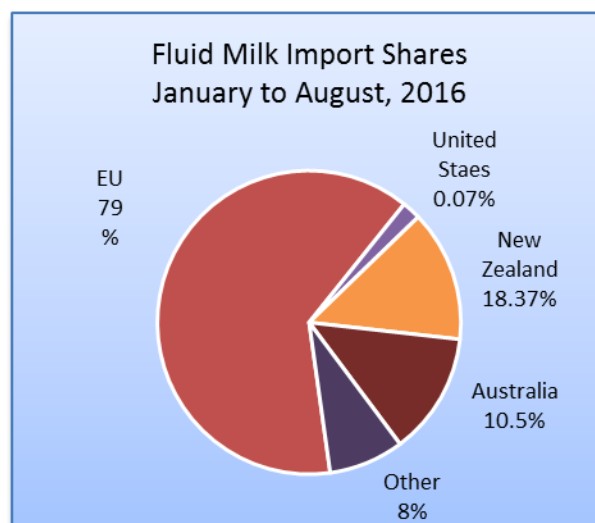
Flow of imported fluid milk will continue to increase in 2017

Post forecasts 2017 fluid milk imports will increase to 900,000 tons, about 38 percent higher than 2016. Although the EU and New Zealand started to curb their production, thus increasing the costs of imported milk, the rise in imported milk prices is expected to happen slowly. Because the imported Ultra High Temperature (UHT) milk price is currently lower than the domestic fresh milk price and Chinese consumers are still wary from past food safety scandals, Chinese consumers continue to prefer imported fluid milk. In addition, imported UHT products are shelf-stable, making them a convenient beverage for young, urban consumers.

Both the EU and New Zealand continue to expand their market share in China, aided by significant Chinese overseas investment in dairy herds and dairy processing facilities. Like many facilities acquired by Chinese investors, the majority of production is exported back to China.

The EU will continue to be the largest single exporter to China in 2017 as a result of the continued Russian ban on EU dairy imports. The overall production from the EU may be reduced slightly in 2017, but government stocks still need to be released back into the market. Accordingly, Post forecasts exports from the EU to China will remain stable. New Zealand remains a popular source for Chinese investment. The lower price and recognized safety factor will continue to attract Chinese investors to invest in New Zealand's dairy industry.

The United States remains a minor player in the Chinese fluid milk market, with less than one percent of market share. U.S. imports are constrained in part by new food safety regulations that stifle U.S. exports to China. The main culprit is China's new registration regulation requirements which can keep new exporters out of the market for years while awaiting regulatory approval (see Import Policy). Once this regulatory bottleneck has been resolved, U.S. imports of fluid milk are expected to increase, due to overall good perceptions about the high quality and safety of U.S. food products in China.



Source: China Customs

Import Policy

U.S. producers who want to export to China must comply with Decree 145, administered by China's Certification and Accreditation Administration (CNCA). Since the implementation of Decree 145 in 2014, many U.S. companies have noted delays in getting their dairy plants and products registered. For further background information, please see the following GAIN report [Registration of Overseas Food Manufacturing Facilities](#) and visit the U.S. FDA website for registration guidance at:

<http://www.fda.gov/food/guidanceregulation/guidancedocumentsregulatoryinformation/importexports/ucm378777.htm>

Whole Milk Powder PS&D table

Dairy, Dry Whole Milk Powder Market Begin Year	2015		2016		2017	
	Jan 2015		Jan 2016		Jan 2017	
	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post
China						
Beginning Stocks	300	300	145	350	0	150
Production	1300	1617	1375	1375	0	1400
Other Imports	347	347	375	400	0	460
Total Imports	347	347	375	400	0	460
Total Supply	1947	2264	1895	2125	0	2010
Other Exports	4	4	2	2	0	0
Total Exports	4	4	2	2	0	0
Human Dom. Consumption	1798	1910	1843	1973	0	2010
Other Use, Losses	0	0	0	0	0	0
Total Dom. Consumption	1798	1910	1843	1973	0	2010
Total Use	1802	1914	1845	1975	0	2010
Ending Stocks	145	350	50	150	0	0
Total Distribution	1947	2264	1895	2125	0	2010

(1000 MT)						

Production

Production of WMP will be stable in 2017 at about 1.4 million tons. Post forecasts the milk price in China will start to recover in 2017, but the rate of recovery will be slow. In the first half of 2016, almost every dairy company in China was converting fluid milk into WMP to deal with the production surplus and low milk prices. In 2017, the WMP production will be back to normal. The WMP production in China is also affected by imports. Although WMP utilization will likely increase in 2017 (see WMP section below for more), such an increase will largely be filled by imports versus domestic production.

Currently, imported WMP is two-thirds the price of domestic WMP, with double the shelf life. The imported WMP cost advantage may narrow in 2017, but is expected to continue asserting a chilling effect on domestic production.

Consumption

Consumption continues to increase in 2017

Post forecasts 2017 consumption of WMP at 2.01 million tons, a two percent increase over 2016. Although utilization of WMP for milk beverages and reconstituted milk is expected to decrease in 2017, due to lack of innovative milk beverage products and lack of consumer awareness of reconstituted milk, WMP usage in yogurt and bakery products is expected to rise. Overall, the growth in these two categories will surpass the reduction on the milk beverage and reconstituted milk usage. In addition, infant formula usage is expected to decrease slightly in 2017, with large Chinese companies heading overseas to establish infant formula plants and then exporting product back to China.

Approximate Whole Milk Powder Usage in China in 2016	
Infant formula	35% market share
Milk beverage	20% market share
Reconstituted milk	28% market share
Yogurt	7% market share
Bakery products	10% market share

Source: Industry Publications

Trade

Imports continues to increase in 2017

Post forecasts WMP imports at 460,000 tons in 2017, about 15 percent higher than in 2016. New Zealand continues to dominate the WMP import market with over 90 percent market share. Chinese dairy facilities produced a significant amount of WMP in the first six months of 2016 that needs to be consumed by the first quarter of next year, based on the shelf life. However, any increases in demand for WMP will be met primarily through imports, due to lower prices, longer shelf life (imported WMP can be stored for up to two years, instead of one for domestically produced WMP), and rigorous food safety

standards. However, this price differential is expected to decrease as New Zealand slowly reduces its milk production in 2017.

In addition, another important factor contributing to increased WMP imports is the continuing Chinese investment in overseas dairy facilities, mainly in Australia and New Zealand. These newly acquired facilities send the majority of their production back to China, further cementing their market position in China.

Exports

China exports a negligible amount of WMP. Post forecasts that exports will remain at 2,000 MT in 2017, with most exports heading to Hong Kong, North Korea, and Myanmar.

Nonfat Dry Milk (also referred to as Skim Milk Powder) PS&D table

Dairy, Milk, Nonfat Dry Market Begin Year	2015		2016		2017	
	Jan 2015		Jan 2016		Jan 2017	
	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post
China						
Beginning Stocks	0	0	0	0	-	0
Production	45	45	40	40	-	40
Other Imports	200	200	210	180	-	180
Total Imports	200	200	210	180	-	180
Total Supply	245	245	250	220	-	220
Other Exports	1	1	0	0	-	0
Total Exports	1	1	0	0	-	0
Human Dom. Consumption	244	244	250	220	-	220
Other Use, Losses	0	0	0	0	-	0
Total Dom. Consumption	244	244	250	220	-	220
Total Use	245	245	250	220	-	220
Ending Stocks	0	0	0	0	-	0
Total Distribution	245	245	250	220	-	220
(1000 MT)						

Production

Production of nonfat dry milk (also referred to as Skim Milk Powder, or SMP) forecast to be flat in 2017

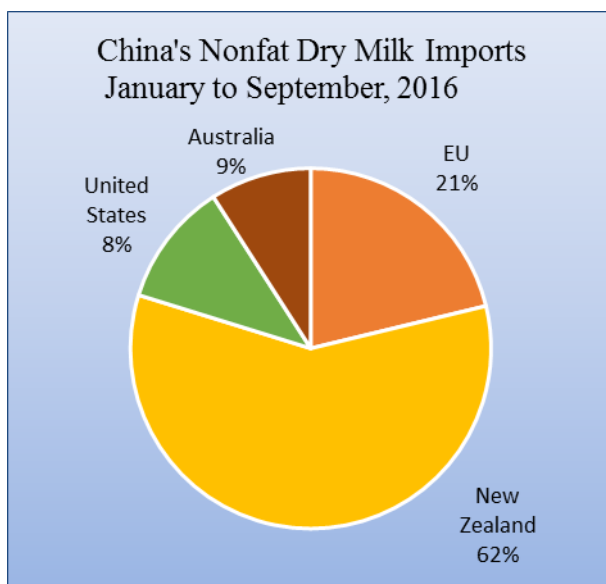
Post forecasts the production of SMP to be steady in 2017 at 40,000 MT. Unlike WMP, China has more limited production of SMP, the majority of which is consumed domestically by dairy processors and is not for outside sales. Despite the continuing increase in demand for infant formula, new Chinese policies effectively constrain major domestic production increases. See below for Policy.

Consumption

Post forecasts 2017 consumption at 220,000 tons, unchanged from 2016. SMP is mainly used in infant formula and milk beverage drinks. Milk beverage consumption has been decreasing due to lack of new and innovative products.

Trade

Post forecasts 2017 imports at 180,000 tons, the same as 2016. As a result of China's limited SMP production, China relies on imports to meet demand in the food processing and infant formula sectors. The majority of imports are sourced from New Zealand and the EU.



Source: China Customs Data

Policy

On June 6, 2016, the China Food and Drug Administration (CFDA) announced the Administrative Measures for the Registration of Recipes for Formula Powder Products for Infants and Young Children (CFDA Decree 26). While announcement stated that the new rules would become effective on October 1, 2016, CFDA has indicated that it is still in process of rolling out the new regulations and has moved the effective date to January 1, 2018. The measures provide requirements and procedures for registration of infant formula recipes, and elaborate on the requirements for labeling and product descriptions. For details, please refer to the following GAIN report: CFDA Publishes Measures for the Registration of Infant formula Recipes (CFDA Decree No. 26) and the link is as below:

http://gain.fas.usda.gov/Recent%20GAIN%20Publications/CFDA%20Publishes%20Measures%20for%20Registration%20of%20Infant%20formula%20Recipes_Beijing_China%20-%20Peoples%20Republic%20of_6-17-2016.pdf