Agriculture and Agri-Food Canada / Agriculture et Agroalimentaire Canada

Canada

The Beverage Market in Yangzi Delta Region

Canadian Consulate General, Shanghai

August 1999

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Introduction

Import opportunities exist in China for a variety of beverages, both non alcoholic and alcoholic. Demand for fruit juices is increasing at a significant rate, as they become more popular with younger Chinese people looking for healthy alternate products. Bottled water sales are also increasing. Beer and wine imports are increasing rapidly, as local products are perceived to be of low quality.

Non Alcoholic Beverages

There are a great variety of non-alcoholic beverages available in the China market. Some popular drinks include mineral bottled water, pop, fruit juice, tea-based drinks, and soya milk. According to the China Beverage Magazine, soft drinks are the most popular beverage among Chinese besides tea.

- **Soft Drinks**

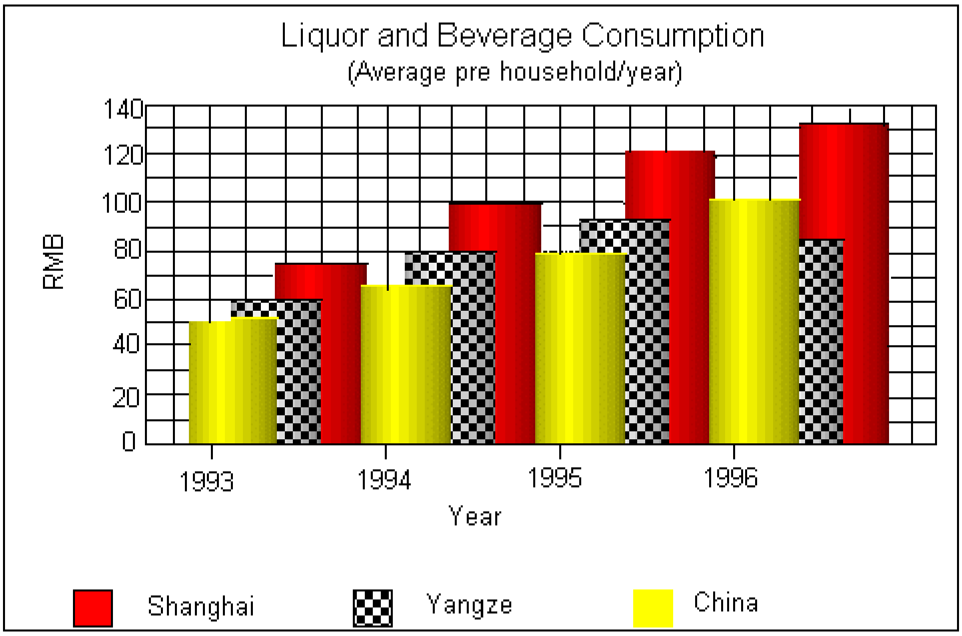
Soft drinks are appealing to the young generation (18 - 35), who also have the most spending power among all age groups in China. While there is the presence of different selections of soft drinks like 7-Up, Pepsi, Ginger ale and many others, Coca Cola is the leading soft drink supplier in China, owning over 25% of the non-alcoholic drinks market. In addition to being one of the first foreign investors in China they are also one of the most successful companies in the China Market.

Tea-based drinks are popular alternatives to soft drinks. Most popular tea drinks are produced by local Chinese or Taiwanese companies, who have probably one of the best understanding of local consumers taste.

- **Fruit Juices**

Fruit juices are becoming popular in the market as Chinese people become more health conscious. Traditionally, local Chinese people preferred coconut and watermelon juices over the apple and orange juices that North Americans and Europeans enjoy.

Some foreign juice companies that have entered the Shanghai area market are American Dole and Great Lakes from Australia. Dole fruit juices are sold throughout supermarkets and chain stores in Shanghai. Dole's headquarter is in Hong Kong but, they have an established manufacturing operation in Huizhou, Guangdong which packages their juices for retailers in China.



Source: 1997 China National Statistics Yearbook

- **Alcoholic Beverages**

Beer consumption has been rising in China for several years. Domestic brands such as Tsing Tao are among the most popular brands for Chinese consumers. Foreign brands like England's Bass, Denmark's Carlsburg, Australia's Foster, Philippines' San Miguel and United States' Miller, Blue Ribbon, and Anheuser-Busch are also very popular and successful in China. These beer companies have joint ventures with Chinese breweries throughout China to produce their brand of beer.

- **Beer**

In January 1997, new Chinese laws governing brewery production ruled that Sino-foreign joint ventures would be restricted to 30 percent of China's total beer production and foreign beer brands would be limited to 10 percent market shares in China. This way local and state owned breweries will be protected from foreign competition, and maintain a majority share in China's beer market.

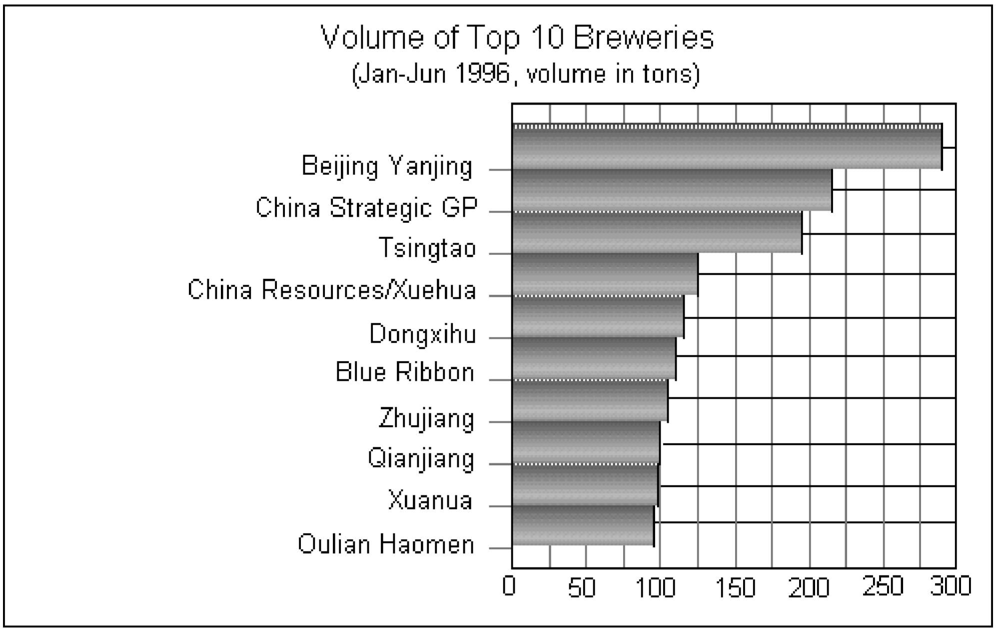
Foreign companies like Danone, a traditional dairy product producer from France, has also entered the beer market to produce Chinese beers. Their objectives, however, is not to make their brand of beer but team up with a local Chinese brewer, improve quality of the local beer, and charge a higher price for the improved beer. This way, they will be protected from foreign competition and gain some profits.

This is a common strategy that foreign beer companies are practising. The benefits are mutually beneficial: the local brewer benefits from Danone's management capital, expertise, modern brewery technology and equipment; and, Danone uses the revenue from the profit for other investments.

Danish beer maker Carlsberg, Australia's Foster and US' Miller also have established joint ventures with local beer brewers in Shanghai, Guangzhou and Tianjin to produce local brand beers. Some of the locally produced beers are exported to Hong Kong, Australia, and other parts of the world. This type of business has been found to be more profitable than simply producing and selling foreign brand beer in China.

In general, beer sales are strong but most foreign beer companies are losing money. Australia's Foster, for example, lost U$8.5 million in the second half of 1996 compared with U$5.6 million during the same period the previous year. Foreign companies have to pay huge costs and must operate on such economies of scale that they need to sell large volumes of beer to break even.

The only exception is perhaps Germany's Beck Beer Company, which is turning a profit in the market. But, they are not producing their premium beer, owning factories and other assets or controlling distribution. They have a license agreement involving technology transfer with a brewery in Fujian province.



Source: The Brewery Council, China 1996

- **Wine**

In the past, hard Liquor was the drink that the rich and powerful people offered to their guests in social settings. This trend has changed, and replacing this is wine drinking. The popularity of wine grew in early 1996, as a result of efforts by the central government to reduce the production of grain spirits, which use up some 12 million tons of valuable food stock per year. The affluent and sophisticated urban middle class in China believes that drinking wine is more classy than brandy; and, the people's changing attitude, that resulted from major media attention and promotion by Hong Kong and other Western countries, that wine drinking, in moderation, was healthy.

Wine sales are concentrated among rich young Chinese consumers. The mass market will be elusive until import tariffs fall sufficiently to enable retail prices for quality wines to an amount low enough to entreat mass consumers, RMB 60 (USD$ 7).

Many foreign wineries, in the attempt to reduce cost, import wine in bulk and bottle locally, like Australian's Jacobs Creek. Other companies like Solvex, a small company, distribute a range of good quality Bulgarian wines whose original purchase price is so cheap that, despite high tariffs, they retail at affordable prices, RMB 50-60 (USD$ 6-7).

The wine market only accounts for a tiny proportion of national alcohol sales and is dominated by several joint venture wineries and a few local wine brewers. Leading imported wines are from France, Germany and Italy. There are wines from Australia, the United States, Spain, and other countries too but, in terms of recognition, France, Germany and Italy are considered best wine producers in China.

Local Chinese brand wines competing with imported wines are "Imperial Court" and "Dynasty". They predominate the market with high sales volume by offering their mass-market quality products wines at low price. The quality of their wines is inconsistent and is not considered comparable to the quality of foreign wines.

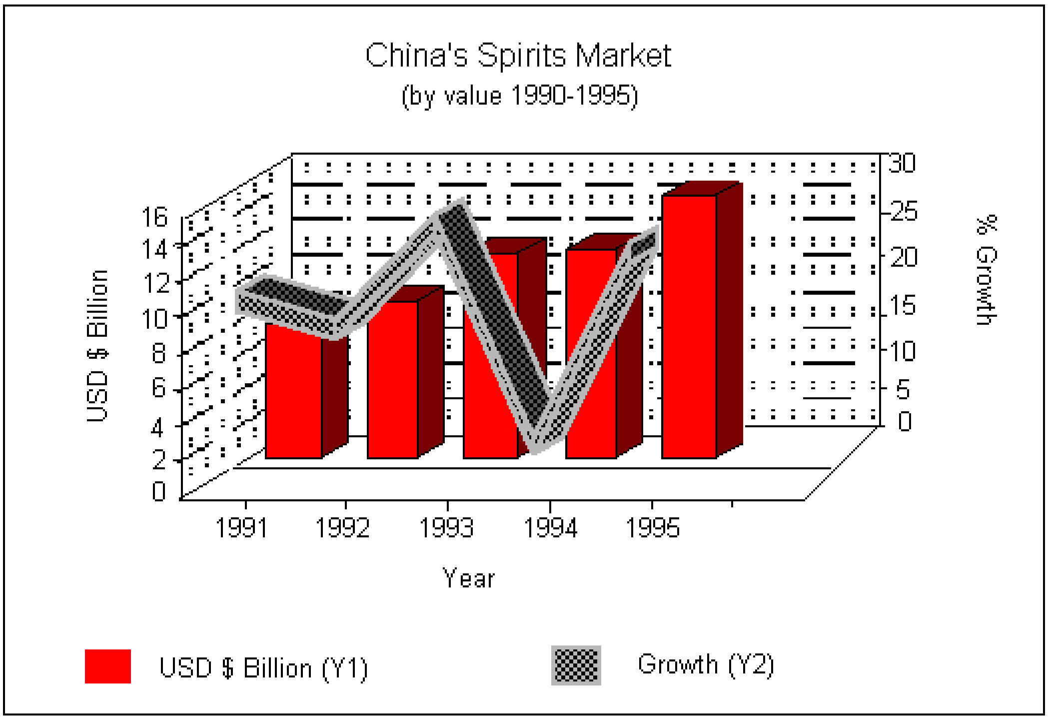
Although imported wines are more expensive than local wines they are preferred by the expatriate community, affluent and wealthy local Chinese people who frequent the high-end restaurants, hotels and supermarkets, particularly those living in Beijing, Guangzhou, and Shanghai.

Consumer Behaviour

- **Non-alcoholic Beverages**

Local Chinese consumers are beginning to be aware of the importance of quality and if they can, they are willing to pay extra for the quality products. Meanwhile, price is still the major factor influencing purchasing decisions for beverages by local consumers. Some companies, like Coca Cola and Australia's Jacob Creek set up their own bottling and production plants in China, to avoid paying high tariffs on their imported drinks and, in doing so, reduce their costs to be able to offer a relatively low price for their beverages.

Aside from price, taste is the next factor influencing purchase decisions for consumers. To ensure that imported beverages are compatible with local tastes, preliminary taste tests are usually required to find out whether beverages that are entering the market for the first time should be modified to suit local consumer tastes. For example, Coca Cola did preliminary taste tests before entering the China with their current pop drink. And, as pursuant to findings from their taste tests, they modified Coca Cola soft drinks to be sweeter to suit local taste preferences.



Source: Data monitor

- **Alcoholic Beverages**

With regards to wine, brand or country recognition is very important. Unlike France who is known by the

Chinese local people as great wine makers, Canada is not recognized for such a trait. "Does Canada produce wine?" local consumers asks when supermarket managers surveyed them for their opinion of Canadian wine.

When French companies entered the China Market with their wines they invested a lot of money for advertisements and promotions to introduce and support their wines. In the beginning, the wines made little profits. Over time, the French companies built a good reputation for their wines, which the consumers quickly associated as a characteristic of France--good wine producers. French wine also came into the market during a time when China began supporting wine drinking as a health benefit. So, wine consumption demand was already increasing in the China Market. Importantly, the French companies had the supply of wines to meet growing wine consumption demands.

In order for Canadian wines to grasp shares in the wine market, they should know for sure that they have the wine supply to meet local market consumption needs. Because, it would be disastrous for a company to promote and advertise their wine products and not be able to supply local consumers' needs. Once supply is available, the company can gain visibility to the market through various forms of consumer and distributor education. It is important to offer local Chinese consumers taste samples to introduce the products and continue to provide consistent good quality products.

Barriers to Entry

Non-alcoholic Beverages

- Tariffs for non-alcoholic drinks range from 15%, for natural waters, to 75%, for sugar or flavour added water, plus 17% value added tax.

- Carbonated drinks (Coke, Pepsi and other pop drinks) are over supplied in the China Market. As a result, export companies representing and/or producing carbonated drinks require special permission from the local government to invest in China. However, non-carbonated drinks (eg. fruit juices) do not require special permission to enter the China market.

Alcoholic Beverages

- Import licenses are required to import wines from overseas. Exporters need to locate and work with a local importing company with the license to import wines. Once the wine is in the country a domestic sales license is also required to trade and distribute the wines in China. Wholesalers and agents who distribute wines must possess the licenses as well as retailers who sell wines to end-users.

- While prospects for imported alcohol vary by sector, foreign players share similar views on the barriers. They argue that import tariff cuts would not only help them reach ordinary Chinese consumers, but would also greatly boost the government's revenue by curbing smuggling and increasing the income of state run import firms.

- Current tariffs for alcoholic beverage range from 40% to 70% plus a value added tax of 17%.

- A major concern for foreign alcohol companies is the Chinese Labelling Law, effective September 1st 1996, which requires imported foodstuffs to carry labels in Chinese stating the product name, ingredients, date of production, net weight, expiry date, method of storage, country of origin, importer and manufacturer. Although the law was intended to bring order and help curb smuggling, inconsistent implementation has resulted in confusion, caused distribution delays and created new opportunities for smugglers.

Critical Concerns

- Government exerts controls that limit distribution to Chinese or joint venture operations, and maintains a shield of protection over local state-owned enterprises.

- Distribution is a problem that all foreign companies experience in the China Market. China lacks good infrastructure, distribution networks, and storage equipment to transport goods between locations. There is also lack of an efficient and effective monitoring system that prevents retail outlets from tracking incoming deliveries of their supplies.

For more detailed information, please refer to our "Food Distribution Systems in the Yangzi Delta Region" report, available through the Canadian Consulate General, Shanghai.

Conclusion

Although alcoholic and non-alcoholic beverages in the China Market are somewhat controlled by the Chinese Government to protect local beverage producers, there is still a large market available for Canadian companies with good quality beverages to enter and reap attractive returns.

Issues Canadian companies need to consider are: high tariffs, poor distribution, infrastructure, and storage facilities, labelling law requirements, limited access to market and product taste modifications, if necessary.

The benefits are: a burgeoning market of more than a billion people, who are adventurous and have more disposable income to buy good quality Canadian non-alcoholic and alcoholic beverages.

Follow Up

The Canadian Consulate General's Agriculture and Agri-Food Office maintains ongoing relationships with local importers, wholesalers, agents and outlets. The office also organizes and participates in numerous promotional activities aimed at generating business for Canadian firms in this sector. Firms interested in taking advantage of these relationships and activities in their efforts to do business in this market would be well advised to stay in touch with us, as follows:

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Publication Date: 1999-08-01