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Packaged food market in China: Part I: Confectionery

Food consumption takes up 1/3 of the Mainland consumers' total living expenditure on average. Food plays a central role in Chinese culture, social life and business relationships. The food market in China is huge and it offers tremendous business opportunities.

The general picture of China's food consumption has been presented in Issue 3. In this paper, the focus will be on the fast growing packaged food products. Packaged food sector is a very broad sector embracing a vast variety of food products. This paper will give a detailed account of the confectionery (including the sugar confectionery, chewing gum and chocolate markets), biscuits, instant noodles and edible vegetable oil sectors.

I. Confectionery

1. Confectionery consumption in China

China's retail sales of confectionery is expected to reach 41.0 billion yuan in 2005, an increase of 6% from 2004, according to Euromonitor (a global market research company) estimates. With a population exceeding 1.3 billion, China is a big potential market for confectionery. At present, market penetration of confectionery in China is still low. According to industry estimates, China's per capita confectionery consumption is only 0.7 kg, which is 1/10 of the level in developed countries and 1/4 of the global average. There is plenty of room for further growth. Not only are there growth opportunities from developing a wider variety of products, but also geographical expansion within the country still has a long way to go before reaching saturation.

China National Commercial Information Centre
Statistics Department, Room 2440, Building 2, No. 25, North Yuetan Street, Beijing, China. Postcode: 100834
Tel & Fax: (8610) 6839 2440, (8610) 6839 2441
E-mail: nmb2000@263.net
Contact person: Ms Syue Bing

Li & Fung Research Centre
Member of Li & Fung Group
13/F, LiFung Centre, 2 On Ping Street, Shatin, Hong Kong.
Tel: (852) 2635 5563 Fax: (852) 2635 1598
E-mail: lfdc@lf1937.com http://www.lifunggroup.com/
Contact person: Ms Freda Tong and Ms Francesca Lim

With rising living standards along with the robust economic development, Mainland consumers' spending on confectionery is expected to rise further. Higher living standards and better health education are driving consumers towards better quality confectionery. Mainland consumers are becoming more selective and cognizant of quality confectionery products. Fancy packages, gift packs and luxury items are widely available in stores and preferred by many customers.

The improved distribution channels and the expansion of retail chain stores have helped confectionery products to extend the consumer reach and broaden the consumer base in China. Meanwhile, increased television and other forms of advertising have helped raise consumers' awareness of confectionery products.

Besides, China is experiencing the "Little Emperor" phenomenon in which one child receives the exclusive care of two working parents, along with two sets of grandparents This phenomenon has considerable impact on the growth of the confectionery market. These children spend, on average, more than US$1 every week on snacks. As parents are increasingly concerned about the problems of obesity and tooth decay among children, health-oriented confectionery products are expected to be in great demand.

Confectionery also plays a special role in Chinese culture – it is a gift item of choice. When Chinese visit family and friends, particularly during holidays like Nation al Day (October 1), Labor Day (May 1), Children's Day (June 1) or New Year's Day (January 1), the most popular gift they bring for hosts is a box or a bag of candy or chocolate. The Chinese New Year, in particular, is the peak candy sales season. Many confectionery manufacturers record up to a third of their annual revenues during the month preceding the festival. Today's candy gifts are far more diversified and starting to include chocolate bars and boxes, soft candy, gummy candy, jelly candy and toy packages.

Many of the confectionery products are small-packaged for on-the-go consumption. A market survey revealed that small-packaged confectionery consumers are less price-sensitive and impulsive buying is prevalent. 30% of the consumers indicated that they pay little attention to the product prices and another 29% simply grab the product without considering the price. Major consumer segment of small-packaged confectionery is the middle-income female aged below 30. Average spending on one time purchase of small-packaged confectionery is around 7 yuan in hypermarkets, 6 yuan in supermarkets and 4 yuan in convenience stores.

2. Confectionery consumers' lifestyle attitudes

Confectionery consumers tend to be willing to try new brands. Meanwhile, chocolates and chewing gums consumers are more sophisticated than sugar confectionery consumers—they tend to believe brands can enhance one's status, be more willing to pay more for quality, and have higher expectation on personal success. Chocolate consumers are also the least likely to prefer domestic brands.

3. Confectionery production

According to the China Food Industry Association, China's total confectionary production has exceeded 1 million tones for five consecutive years. In 2005, China's sweet and chocolate production is expected to reach 1.28

million tons with total turnover value exceeding 20 billion yuan. There are over 2,000 sweets and chocolate enterprises in China. Among which, 230 enterprises have an annual turnover value of more than 5 million yuan. The production mainly concentrates in Beijing, Shanghai, Guangdong, and Fujian, etc.

There are a number of small players with limited production capacity and product offerings, and have long relied on competitive pricing strategy in the low-end market for survival. The recent hike in sugar price has brought tremendous pressure on these players. It is expected that some of the weakest players will be eliminated for their already slim profit margins. Stronger players, on the other hand, can withstand the price pressure better and are hoping to use the opportunities to consolidate their positions.

4. Market players

Basically the confectionery market can be divided into three segments: the high-end market dominated by multinational brands and a few domestic brands; the mid-range segments in which a large number of domestic brands flourish; the low-end market with a high concentration of domestically produced anonymous branded products.

In the past decade, rising living standards and the influx of high-quality foreign products has brought considerable changes to China’s confectionery market. The arrival of more newcomers has spurred local manufacturers to reshuffle their current product offerings and formulate new marketing strategies to meet consumers’ ever changing needs. To survive the intensifying competition, local players are prone to improve their operation scale, expand their types of product offerings and innovate new flavors.

Currently, multinational companies take the lead in the upper-end of China’s confectionery market. Their success is mainly attributable to their superior and distinctive product quality and taste, strong promotional and brand building efforts. Having entered the Mainland market for more than 10 years, some big foreign confectionery enterprises have already gained a deep understanding of the market and have been aggressive in developing new products and new distribution channels. Besides, having set up their own factories in China, foreign players such as Effem Food (Beijing) Co Ltd (the brand-owner of Dove, M&M’s, Snickers, Skittles and Maltesers, etc.) and Cadbury Food Co Beijing have reduced their costs and thus made their products more affordable to the mass consumers. However, the market share of these foreign players is still very small and the whole market presents a fragmented picture with a large number of local manufacturers in the mass markets, especially in the less-developed cities and the rural regions.

While the more expensive foreign brands center on the big cities, well-known domestic players are more popular in smaller cities and rural areas, where people have much lower disposable income levels. Some of the famous ones include Shanghai Golden Monkey Co, Fujian Yake Food Co Ltd and Guan Sheng Yuan Group. Many of these enterprises have deep penetration in the country, even in some developed rural areas. Shanghai Golden Monkey Co, for instance, focuses on second- and third-tier cities and the developed rural areas, and has very impressive volume sales in these regions. But as the unit prices of its products are quite low, the company’s value sales is much lower than its volume sales.

During the past years, the big domestic confectionery enterprises have been gearing up to upgrade their production and safety-monitoring capabilities. For example, Yake, Shanghai Golden Monkey, Guan Sheng Yuan and Le Conté have imported advanced production equipment from Germany, Italy, Belgium, etc., to improve production efficiency and raise the level of production automation. These enterprises have also put in abundant resources in research and development to better meet consumer demands.

Establishing extensive sales network and exploring new distribution channels for the confectionery products are other ways to win market share. Shanghai Golden Monkey Co Ltd, for example, has set up over 2,000 sales counters and stores in hypermarkets and supermarkets nationwide, and this has greatly increased its market penetration. Apart from that, it has initiated China's first specialty store for its sugar confectionery in Jinan (in Shangdong province). With its own distribution channel, the company is able to save a large amount of entry fees paid to supermarkets or hypermarkets. It also enables the company to monitor sales and collect sales revenue in a more effective and easier way. However, confectionery specialty stores remains a niche distribution channel in China. The explosive growth of supermarkets and hypermarkets in China has made the future of chained confectionery specialty stores less promising than expected.

The China Food Network has identified the top 10 confectionery enterprises in China (see Exhibit 1).

Exhibit 1: The top 10 confectionery enterprises in China, 2005

China Golden Monkey Group (金絲猴集團有限公司)
Dongguan Hsu Fu Chi Food Co Ltd (東莞徐記食品有限公司)
Effem Food (Beijing) Co Ltd (愛芬食品（北京）有限公司)
Fujian Yake Food Co Ltd (福建雅客食品有限公司)
Golden Crown Co.,Ltd (金冠食品有限公司)
Labixiaoxin (Fujian) Foods Industry Company Limited (臘筆小新(福建)食品工業有限公司)
Perfetti Van Melle Confectionery (China) Co Ltd (不凡帝范梅勒糖果（中國）有限公司)
Shanghai Guan Sheng Yuan International Trade Co. (上海冠生園食品有限公司)
Strong Group Co Ltd (南京喜之郎食品有限公司)
Wrigley Chewing Gum Co Ltd (箭牌口香糖有限公司)

Source: China Food Network

5. Development trends

(1) Health-oriented confectionery gaining popularity

With improving living standards, more hectic pace of life and better product exposure, the more well off Mainland consumers are becoming more health-conscious and health-oriented confectionery have witnessed dynamic growth in recent years. Generally speaking, quite a number of consumers still perceive negatively about confectionery, which are thought to bring about tooth problems, obesity and diabetics. Thus, health-oriented confectionery is likely to be more popular among the Mainland consumers. As the market is more likely to embrace health-oriented products, manufacturers are making more efforts to change consumers' negative image of confectionery by adding more nutritious ingredients or avoiding unhealthy ingredients in confectionery products. Dynamic new launches in health-oriented confectionery, at the same time, are spurring the sector sales.

Functional gums, vitamin-fortified confectionery, and reduced-sugar confectionery are the growth drivers of health-oriented confectionery. Xylitol is the most popular ingredient for chewing gums, while vitamins are most popular in fortified sugar confectionery. Over the past few years, more than 10 chewing gum producers have launched Xylitol-fortified chewing gums fortified. Since 2003, fortified sugar confectionery has gained widespread popularity with the craze for vitamins. Yake V9 from Fujian Yake Food Co Ltd is a successful example. The product claims to have nine vitamins that are essential to human health. The popularity of this product was further boosted by the SARS outbreak.

Though health-oriented confectionery is becoming increasingly popular, it still represents a small portion of the total confectionery sales. The growth of the health-oriented confectionery is very much being derived from a small consumer base. This can be explained by a number of factors. Firstly, health consciousness among consumers, though growing, is still low. Secondly, the average income level of Chinese consumers is still relatively low, health-oriented confectionery, usually of a slightly higher unit price because of higher-cost ingredients, are not as affordable as those non-health-oriented products. Thirdly, health-oriented confectionery market, as a whole, is still underdeveloped in the country, with a handful of brands and a limited presence of products available in the market. Product knowledge is therefore low among consumers in general.

All in all, the growth of health-oriented confectionery in China is expected to outpace the total confectionery sector's growth with China's dynamic economic growth and improving living standards. Many manufacturers have been making efforts to narrow the price gap between health-oriented products and standard ones, in order to attract more consumers. Some of them are trying to make the health-oriented confectionery products in smaller package sizes, so as to minimize the impact of price hikes. For example, Wrigley Chewing Gum Co Ltd kept the retail price of newly launched Juicy Fruit (with fortified Vitamin C) almost at the same level as the old one, though the package size is slightly reduced by 1.5gram.

Meanwhile, some sugar confectionery enterprises are further exploring the creamy candy market. The concept of creamy candy being good for health and having high nutritional value is widely promoted. Some popular slogans include "Three pieces of its creamy candies is equivalent to a cup of milk" and "Two pieces of creamy candies per day help supplement the vitamin intake". This strategy helps these enterprises to differentiate their products by attaching additional functional value and is successful in attracting health-conscious consumers.

(2) Great potential in the less developed rural market

Competition is less intense in the rural market, which offers great potential, especially for mid-range products. Currently, the most prevalent confectionery products in the rural markets are mainly low-end products from local players. As income rises in the rural areas and the government accelerates its plan to boost rural consumption and facilitate rural retail infrastructure development, confectionery consumption in rural areas is expected to grow.

(3) Increasing product development, brand building and marketing efforts

The competition in China's confectionery market is intense. In order to win market share, players have been devoting more and more resources in product development, brand building and marketing to better meet consumer demands and create product differentiation. In recent years, a wide variety of new products with different flavors and added-functional values have been launched which have greatly enriched the product structure of China's confectionery market. New product types and tastes and an increasing number of health-oriented and functional confectionery products can now be found in China. Fruit-flavored sugar confectionery products, though still dominate the market, are gradually losing ground to other special flavors such as sesame, peanut, coffee, green tea and liqueur.

Beside taste and price, packaging is another crucial factor affecting purchasing decision. Consumer-friendly packaging encourages sales. Bulk packaging of chewing gums for office or home consumption, smaller packaging of sugar confectionery for impulsive purchase and on-the-go consumption, as well as exquisite packaging of chocolate as a wedding door gift are likely to appear more inviting to consumers. Some traditional confectionery enterprises are also making ways to repackage their products into a more inviting style. The traditional Guan Sheng Yuan Group Co Ltd has done a great job in revamping and repackaging its products. After three years of market research and product development, the sugar level of its famous White Rabbit products has been reduced and calcium has been added to cater to the changing tastes of the younger generation. A new packaging as a standing rabbit has also been launched for the traditional White Rabbit products. The new packaging has attracted a lot of attention from consumers.

Moreover, confectionery enterprises have been increasing their brand building and marketing efforts instead of just competing in price. Over 50 million yuan is expected to be spent on China Central Television (CCTV) commercials by sweet and chocolate enterprises in the first half of 2006. This reflects that brand building has become a prominent expansion strategy of many confectionery enterprises. For the period from January 2003 to June 2004, Yake and Shanghai Golden Monkey have devoted the largest sum in CCTV commercials. Yake spent a huge sum of 60 million yuan in its advertisement. Apart from paying to CCTV, several million yuan have been paid for the production costs of the commercials and hiring popular actress as spokesmen. Yake has recorded notable success after placing advertisements in CCTV's prime time slots. Five days after Yake's advertisements were shown in CCTV, the sales of its product V9 skyrocketed. It is reported that its distribution agents increased their one-time order quantity from 50-60 boxes to 500-600 boxes, some even ordered 2,000 boxes. Riding on this success, Yake products have successfully made presence in thousands of hypermarkets, supermarkets and convenience stores including Hualian, Lianhua, Metro, Lotus and Nongongshang.

(4) Confectionery as a gift of choice – wedding confectionery

There is a huge potential market for confectionery gifts, especially wedding confectionery. According to an online survey conducted by a Mainland wedding confectionery enterprise, around 18 million couples get married in China every year. If each couple spends 200-300 yuan on wedding confectionery, the consumption value will reach 4-5 billion per year. But the market size should be far more than that. In fact, in some relatively developed regions like Shanghai, Zhejiang and Fujian, each couple spends almost 1,000 yuan on wedding confectionery. Besides, unlike other confectionery gift items whose sales concentrate in festival periods, wedding confectionery sales are not bounded by seasonal factors. At present, a number of confectionery enterprises offer wedding confectionery, but many of them only treat this kind of product as part of their product portfolio and so far, few strong brands have been established in wedding confectionery sector.

Shidi (詩蒂) is a recently emerged brand for wedding confectionery and is highly popular in the eastern area in China. However, Shidi is actually not a wedding confectionery manufacturer, but a wedding service provider. Sources reveal that Shidi outsources the manufacturing process to the OEM (original equipment manufacturing) factories and it only undertakes the design function. Originally, Shidi was only sold in the company's sales offices. Now, its sales channel has been extended to hypermarkets in more than ten provinces across China. All Shidi wedding confectionery is boxed-packaged chocolates. The standard box size is 15-30 grams and the price range is around 1-2 yuan. Wide variety and beautiful packaging makes Shidi a strong wedding confectionery brand in Shanghai and its neighboring regions.

Packaging is extremely important and is a critical selling point of wedding confectionery. Wedding confectionery enterprises can either take up the design role themselves or outsource this function to professional design house. Currently, though many of the good packaging designs are come from Hong Kong, domestic design companies are fast developing.

Wedding confectionery is not a fast-moving consumer good. Its consumption frequency is low, but the consumption volume is high. Thus, unlike other types of confectionery which emphasis volume sales and mass production, wedding confectionery enterprises are advised to offer tailored-made or personalized services in the aspects of packaging and value-added services.

6. Performance of by product sector

Confectionery sector can be broadly divided into three sub-sectors, namely sugar confectionery, chewing gums and chocolate. Exhibit 2 shows the retail sales of the three sub-sectors for the period from 2000 to 2005.

Exhibit 2: Retail sales of confectionery by sub-sector, 2000-2005 (million yuan)

Sub-sector	2000	2001	2002	2003	2004	2005
Sugar confectionery	21,948.2	23,511.8	25,356.6	27,115.9	28,700.1	30,337.0
Chocolate	3,129.0	3,435.8	3,805.7	4,426.5	4,841.7	5,277.4
Chewing gum	3,316.3	3,774.1	4,243.6	4,676.9	5,054.3	5,372.0
Total	28,393.50	30,721.70	33,405.90	36,219.30	38,596.10	40,986.40

Source: Euromonitor

(1) Sugar confectionery

(i) Sugar confectionery consumption

Sugar confectionery remains the largest sub-sector in the confectionery market but its share of the total confectionery market has been slipping in recent years (see Exhibit 2). This is less to do with any weakness in the sector, but more an indication of just how rapidly the other two sub-sectors have grown. Sugar confectionery is indispensable in the traditional Chinese festivals, such as the Chinese Lunar New Year. It is also the mainstay gift for wedding ceremonies in the vast rural areas.

China Marketing and Media Study (CMMS) has been sampling over 70,000 Chinese consumers in 30 major cities. In its 2005 survey, slightly more than one-third of respondents have consumed sugar confectionery over the past year. Penetration[1] is the highest in Chengdu, Guangzhou, Hefei and Chongqing where over half of the respondents have consumed sugar confectionery products. In comparison, consumers in northern cities are generally less enthusiastic about sugar confectionery consumption. Just around one-fifth of the respondents in Beijing, Ha'erbin, Changchun, Shenyang and Dalian have consumed the products.

On average, sugar confectionery consumers have the products 2.6 times a month. Consumption frequency is the highest in Kunming, Suzhou, Hanzhou and Ningbo and the level is nearly the double of the country average. Shenzhen respondents consume sugar confectionery once a month, the lowest level in China.

As the market becomes more mature, product enhancement and product innovation have become the major growth drivers. From late 2003 onwards China witnessed a craze for vitamins. Since then, an increasing number of health-oriented sugar confectionery products, such as vitamin-, calcium- and protein-fortified candies have emerged and captured quite a lot of attention. Effective marketing is also propelling the sector growth. Some big confectionery enterprises have put in massive spending on advertising and achieved notable success.

(ii) Market players and brand performance

Since sugar confectionery has long history in China, many domestic players have already developed to a mature stage. Many of these enterprises have built up strong production capabilities as well as mature distribution channels. Meanwhile, as the entry cost and barriers are low in this sector, the market is very fragmented. There are quite a number of local players whose products may only be found in certain regions. Owing to cheap ingredients and low distribution costs, these local products meet the demand from low-end market, such as in inland cities and rural areas. Amid the intensifying competition, some well-known domestic players turn to alternative way of expansion. Guan Sheng Yuan Group Co Ltd, for instance, signed a contract in late 2003 to provide branded and OEM products for all Walmart's (a global supermarket and hypermarket operator) outlets.

The top 5 most frequently consumed brands in 2005, according to CMMS survey, are Alpenliebe (26.3%), White Rabbit (18.9%), Hsu Fu Chi (15%), Cadbury Eclairs (9.5%) and Golden Monkey (5.8%). Alpenliebe is the leader in 19 cities. Around 60% of the top 5 brands consumers are female. Domestic brands fare less well in the youth segment — Alpenliebe and Cadbury Eclairs are more welcomed by youths.

Dongguan Hsu Fu Chi and Perfetti Van Melle Confectionery (China) Co Ltd are the leading foreign players in the sector. However, they do not have significant value shares in the highly fragmented market environment. Hsu Fu Chi's strengths lie in its extensive distribution network and active new product introductions. Perfetti Van Mella owns the brands Alpenliebe, Mentos Fruit and Fruit-tella. With innovative taste, fashionable packaging and modern product image, Alpenliebe has won much favor from the Mainland consumers.

1 Penetration rate: Number of respondents that have consumed the respective product over the past year/Sample size

(iii) Performance of different sugar confectionery products

Boiled sweets

Looking at the performance of different sugar confectionery products, the traditional types of sugar confectionery – boiled sweets – still account for the largest market share. Due to its low retail price, it is highly popular in rural areas. As market entry barrier for boiled sweet production is low, there exist a vast number of boiled sweet manufacturers but their product quality varies a lot and many of them only serve the regional markets. The profit margin of boiled sweets manufactures is low as little technical skill is involved in production. In recent years, the growth of boiled sweets is decelerating due to the lack of product innovation and effective marketing. The strong competition from other fast developing products such as mints and medicated confectionery, gums and liquorices is also attributable to the slowdown of growth. With growing product homogeneity in the sector, innovative flavors or added values are going to be the key winning factors. Some famous boiled sweet brands include Oishi, Yake, Golden Monkey, Golden Crown, etc.

Soft candies

For soft candies, the market is very fragmented without a leading player. Want Zai QQ of Want Want stands slightly out from the others, followed by Meijue of Yake. Most of the products are small packaged targeting the children's segment. There are numerous small players and the competition is very keen. Want Zai QQ, though is quite popular in China, faces high pressure on profitability due to the small package size and low unit price. In this regard, large-scale operation and volume sales are vital to maintain profitability. We foresee that the small brands will gradually be squeezed out of the market amid the intense competition.

Mints and medicated sugar confectionery

Mints and medicated sugar confectionery products are fast growing. However, the sugar confectionery market is still dominated by fruit-flavored sugar confectionery products and the overall volume and value sales of mints and medicated confectionery are still rather small. Worsening environmental problems may be one of the main reasons behind the dynamic growth. Both the mints and medicated confectionery products provide a convenient means of treating or relieving minor ailments like sore and dry throats. In addition to having the traditional sweetness of sugar confectionery, both help freshen the breath. Breath freshening strips have already emerged in the big cities but they still constitute negligible market share. Key players in mint and medicated confectionery sector include Halls, Mentos, Polo, Lakerol, Qingzui, Clorets, Wrigley and Ricola.

Creamy candies

Creamy candies are also popular in China. White Rabbit is always the top player in the sector. Other competitive brands include Yake, Alpenliebe, Golden Monkey, UHA, Golden Crown and Wo Wo. Health benefit is the key selling point of creamy candies.

Toffees, caramels and nougats

Toffees, caramels and nougats are able to maintain the sales growth, with product innovation and effective marketing to keep pace with the changing tastes of consumers. Toffees filled with chocolate, milk, coffee or something else have been launched to satisfy consumers' changing tastes.

(2) Chewing gums

(i) Chewing gum consumption

According to industry estimates, Chinese consumers on average buy 10 sticks of gum a year, which is far behind the American average of 160 or Taiwan's 70-80. With a population five times that of the United States, there is a lot of room for growth. Being relatively small in volume and value sales, gums posted stronger growth than sugar confectionery in 2005. Meanwhile, new rural markets for chewing gums are gradually opened up with the spread of modern retail chain stores in the countryside. Therefore, we foresee that the sector growth will continue to be positive.

Unlike sugar confectionery and chocolates of which females are the major consumers, chewing gums are slightly more welcomed by males. Also, chewing gum consumers are usually young people. Nearly 60% of the top 3 brands consumers are aged below 35.

(ii) Market players and brand performance

International brands took the lion's share of gum sales. Wrigley Chewing Gum Co Ltd, which offers a wide variety of products and brands such as Extra, Doublemint, Juicy Fruit, Spearmint and Cool Air, is the market leader. According to CMMS, the top 3 chewing gums brands in China are Wrigley's Doublemint, Juicy Fruit and Extra Blueberry. Doublemint is a distinct leader with nearly 80% of the respondents claiming that it is the most frequently consumed brand. It is indeed the most popular brand in all cities covered. Wrigley has established a strong sales network in China with a staggering one million sales points – 30,000 sales points in Shanghai alone. Its products can even be found in inland areas. Furthermore, Wrigley has successfully built up a very positive social image and professionalism by launching its Dental Program in late 2004, promoting teeth-protection and awareness on campuses, in the community, and in hospitals. Together with Wrigley's systemic new product launches and aggressive marketing efforts, it has established a strong foothold in the gum sector.

Lotte China Foods Co Ltd is a distant second in China's chewing gum sector. It has been outstanding in using drugstores as a distribution channel for its gum products. Also, Lotte was the first company to adopt bottle-packaged Xylitol products in China. All these, together with Lotte's active participation in social activities such as teeth protection activities, have greatly enhanced its market share and boosted its brand image.

(iii) Performance of different types of chewing gums

Sugarised chewing gums

Sugarised chewing gum is the mainstay of the gum sector. Due to its lower unit price, sugarised gum has a larger consumer base in China and is extremely popular in second- and third-tier cities. Mint, especially peppermint and spearmint, is the most popular flavor in China. This is followed by fruit flavors, including juicy fruit, lemon, apple, strawberry and blackberry, etc. Generally female consumers are more in favor of fruit flavors than their male counterparts. As consumers become more affluent and health-conscious, sugarised gums are expected to lose ground to functional gums and sugar-free gums gradually.

Functional and sugar-free gums

Chinese consumers, especially those in big cities, are increasingly fascinated by functional and sugar-free gums, which also seem to be the key focus of manufacturers. Their practical functions, including tooth decay prevention, whitening, and refreshment have added value to the average chewing gums. Following the functional gum craze in 2004, manufacturers' interest in these products did not wane in 2005. Major players, such as Wrigley Chewing Gum Co Ltd and Lotte China Foods Co Ltd, have actively involved in new product launches as well as marketing activities throughout the year. Lotte China Foods Co Ltd, for example, launched Lotte Xylitol+2 in China in June 2005, which is claimed to be able to prevent and fight against plaque and cavity. The crave for functional gums is expected to continue in coming years. With continual product innovation and manufacturers' aggressive marketing activities, functional gums are likely to achieve further market penetration.

Bubble gums

Bubble gum sales have also grown well, but were much slower than other sectors, largely due to the fact that bubble gums are less appealing to adult consumers and bubble gum consumption has been confined to children.

(3) Chocolate confectionery

(i) Chocolate consumption

Developed countries are the major consumers of cocoa. However, they are mature markets and new growth is likely to come from countries such as China.

At present, global sales of chocolates is estimated to be USD51 billion, while sales in China only accounts for less than 1% of the world total. The per capita chocolate consumption in China is still much lower than the world's average. Statistics shows that Chinese annually consume less than 50 grams of chocolates per person, while in Western Europe, the per capita chocolate consumption is 8 kilograms per year. Even in China's neighboring countries such as Japan and South Korea, average per capita chocolates consumption exceeds 1.4 kilograms a year. CMMS figures show that in 2005, only one-third of the respondents have consumed chocolates over the past year. Shanghai and Hefei both register penetration of around 50%. It is then followed by Hanzhou and

Ningbo. Shenyang, Ha'erbin and Chengdu have the lowest penetration for chocolates. One of the reasons for chocolate's smaller market share is its rather high unit price than sugar confectionery. In China, chocolate confectionery usually consists of high-end products. People in poorer cities and rural areas still treat chocolate as a luxury. Meanwhile, the average consumption frequency is 3 times per month among the consumers. Consumption frequency is 7 times per month in Kunming, the highest in the surveyed cities.

Though China's chocolates market is still smaller than most of the developed counties and its per capita consumption of chocolates is low, the growth rates are impressive and the room for expansion is enormous. With a population of more than 1.3 billion, China's sheer market size has already attracted many foreign players.

There are several growth drivers. First, rising living standards and growing familiarity with chocolate products have brought a rapid increase in consumption. With regard to the average consumers, previous poor knowledge of chocolate as a foreign confectionery and low disposable income are the major hindrance to stronger growth of chocolate in China. Growing consumer exposure in recent years helps boost the sector growth. Now more and more consumers can differentiate between good and bad chocolates. Chocolates are no longer regarded as "black candies" anymore. Besides, with higher disposable income, more and more Mainland consumers opt for more premium brands like Dove.

Second, the tradition of gift-giving in China has attributed to the vigorous growth of chocolates, especially the boxed assortments. Consumption around festivals is a crucial growth driver for chocolate. On festivals such as Chinese Lunar New Year, St. Valentine's Day, boxed assortments are generally regarded as the preferred gifts. Besides, in special occasions like weddings, chocolate confectionary is replacing traditional confectionery as gifts. To tap this market, some players such as Cadbury and Mars have launched wedding chocolates, with festive packaging in "auspicious" red. Seasonal sales of chocolate are usually strong. The best season is winter as chocolate can provide more calories for consumers to keep warm and more importantly, there are several vital festivals for chocolate consumption – Christmas, Chinese Lunar New Year, as well as St Valentine's Day. Value sales in winter, especially around festivals, can be twice the levels in summer.

(ii) The new national standard on chocolates and chocolate products

In August 2004, a new national standard on chocolate and chocolate products took effect to regulate chocolate production and sales in China. The standard regulates that the content of fat in non-cocoa butter cannot exceed 5%. The content of cocoa butter must be no less than 20% in white chocolates and no less than 18% in dark chocolates.

China is estimated to be home to 30 chocolate companies, which produce over 100 types of chocolate products. However, more than 80% of the products do not meet the requirements of the new standard. Currently, domestic producers mainly use non-cocoa butter such as species of cocoa fat and cocoa butter substitutes as raw materials. Though much cheaper than natural cocoa butter, the ingredients have inferior flavors. The new standard puts great pressure on domestic chocolate makers who are already in weak position. In fact, it is high time for domestic players to gear up their efforts. Inferior ingredients could deter consumers from buying specific brands. To survive the intense competition, domestic players should improve product quality, upgrade production technologies, increase investment in R & D and strengthen brand-building efforts.

On the contrary, the new standard, to some extent, is good news to multinationals and prestigious domestic players, for they will benefit from the more regulated market environment and stronger consumer confidence.

(iii) Consumer behaviors

Demographics of chocolate consumers

The young generation is the largest consumer group for chocolates. Sources reveal that younger consumers buy chocolates more frequently. According to China Addictives (a web site specializing on food addictives) statistics, there is a close correlation between age and the frequency of consuming chocolate. Those aged below 35 have high chocolate consumption and they take up a significant proportion of heavy chocolate consumer group. This is consistent with the CMMS findings that above 60% of the top 5 brands consumers are aged 35 or below. Chocolates are also more popular among females. CMMS figures have shown that around 60% of top 5 brands consumers are females.

Purchasing considerations

Statistics of IMI Consumer Behaviors & Life Style Yearbook 2004-2005 (hereafter referred to as "the IMI survey"), a market research surveying over 34,000 Mainland consumers, shows that taste was considered the most important criteria when choosing chocolate (see Exhibit3). Compared with the 2003 survey, one noteworthy trend is found: consumers now place less emphasis on price while attaching more importance on brand and taste. Price used to be the major consideration for Chinese consumers when they went shopping, but now more and more people consider value-for-money. Though imported chocolates are more expensive, most consumers are willing to dig deeper into their pocket for what they regard as worthwhile. As the Chinese consumers grow better off, they are becoming more selective and cognizant of quality chocolate.

Exhibit 3: Key factors affecting consumers' choice of chocolates, 2004

% of chocolates consumers that regard the factor as important

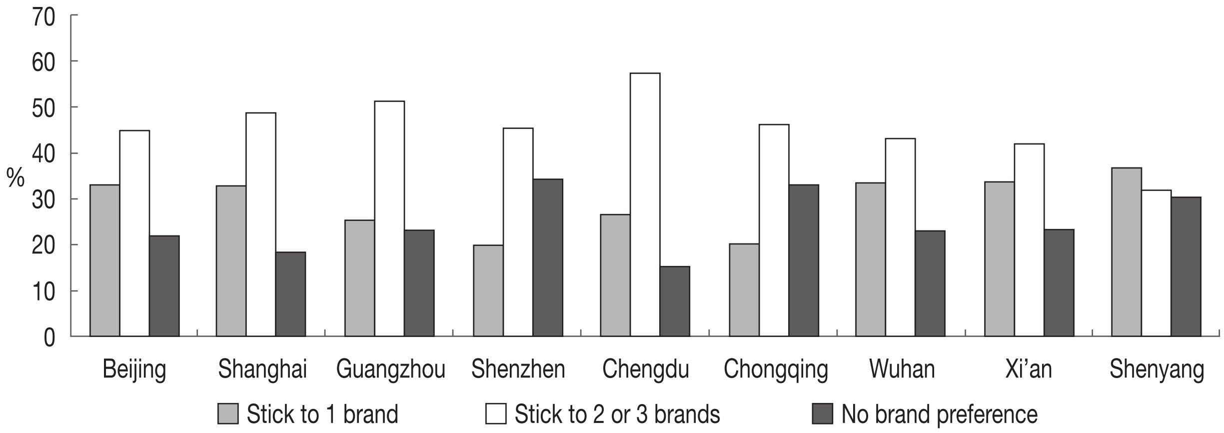
City	Weighted sample size *('000)*	Prices	Brands	Tastes	Buying convenience	Advertising	With special offer	Packaging	Production date	Out of habit
Beijing	3,249	33.1	51.6	77.7	17.0	5.9	3.0	4.0	17.1	11.5
Shanghai	4,843	30.4	63.6	79.1	13.7	12.5	3.5	4.9	15.6	9.0
Guangzhou	1,501	34.9	54.0	65.8	14.6	6.0	8.5	11.1	11.5	6.5
Shenzhen	1,600	23.6	43.9	67.1	18.0	6.1	6.7	7.1	16.7	8.5
Chengdu	1,031	25.0	48.3	75.8	12.2	8.4	7.7	8.6	13.8	10.3
Chongqing	684	25.4	28.8	73.0	15.0	5.3	3.2	4.1	16.8	6.1
Wuhan	1,670	31.3	53.0	71.7	5.5	7.3	4.9	5.7	24.2	8.4
Xi'an	915	29.0	44.5	78.2	8.1	8.3	2.5	8.1	25.2	9.2
Shenyang	1,347	37.0	48.5	71.5	15.3	6.0	5.6	5.3	23.7	6.1
Nanjing	1,166	23.1	49.1	70.1	7.1	4.1	3.9	4.1	13.2	5.7

Source: IMI Consumer Behaviors & Lifestyles Yearbook 2004-2005

Brand habits

The IMI survey shows that in the surveyed cities, most of the chocolate consumers tend to stick to 2 or 3 brands (see Exhibit 4). Chocolate consumers in Chengdu and Shanghai exhibit relatively high brand loyalty, with over 80% of the respondents indicating that they tend to choose from 1 to 3 brands only. In contrast, in Shenzhen, Chongqing, and Shenyang, consumers shows little brand preference.

Exhibit 4: Brand habits of chocolate consumers in selected cities, 2004



Source: IMI Consumer Behaviors & Lifestyles Yearbook 2004-2005

The taste of consumers

As shown in Exhibit 5, original flavor is most popular in all the surveyed cities. This is probably due to the fact that chocolate is still a fairly new product in the Mainland. Consumers have limited product knowledge and are resistant to try special flavors. Flavored chocolates, such as mint, fruit-flavored and whiskey chocolates, remain to be niche products in the market. Milk and dark chocolates and those with nuts are the next three popular types of chocolate. Dark chocolate is lower in fat and it satisfies consumers’ demand in both taste and nutrition. As consumers are more health conscious, dark chocolate is gaining popularity among Mainland consumers. Both international and domestic players have noticed the new trend and launched dark chocolate products. These include UHA Tenong Dark Chocolate by UHA-Mikakuto (Shanghai) Co Ltd and Le Conté Flake Chocolate by Shenzhen Le Conté Foodstuff Co Ltd.

Exhibit 5: Top 5 popular flavors in selected cities, 2004

Flavors and % of chocolates consumers

	Weighted sample size ('000)	First	Second	Third	Forth	Fifth
Beijing	3,249	Original (45.2)	Nuts (26.8)	Milk (20.3)	Dark (19.1)	Wafer (13.3)
Shanghai	4,843	Original (46.1)	Milk (33.0)	Nuts (28.1)	Dark (19.9)	Wafer (6.2)
Guangzhou	1,501	Original (42.0)	Nuts (27.8)	Milk (26.8)	Dark (12.5)	Wafer (5.4)
Shenzhen	1,600	Original (30.0)	Nuts (24.1)	Dark (23.8)	Milk (22.6)	Wafer (10.1)
Chengdu	1,031	Original (47.1)	Dark (26.3)	Milk (24.8)	Nuts (17.1)	Wafer (4.2)
Chongqing	684	Original (36.5)	Dark (28.4)	Milk (20.3)	Nuts (17.7)	With alcohol (4.7)
Wuhan	1,670	Original (56.5)	Dark (34.1)	Milk (22.1)	Nuts (10.9)	Chocolate beans (7.8)
Xi'an	915	Original (41.8)	Milk (26.5)	Dark (26.2)	Nuts (19.5)	With alcohol (4.8)
Shenyang	1,347	Original (49.1)	Dark (22.4)	Milk (21.3)	Nuts (17.2)	Wafer (8.5)
Nanjing	1,166	Original (46.0)	Milk (26.3)	Dark (20.3)	Nuts (15.7)	Wafer (4.0)

Source: IMI Consumer Behaviors & Lifestyles Yearbook 2004-2005

Occasions of consumption

As illustrated in Exhibit 6, chocolate is a popular snack among Mainland consumers. For some consumers, they hold the view that chocolate can bring nutritional benefits and regarded it as health supplement, especially for the consumers in Beijing and Shenyang.

Exhibit 6: Occasions of consuming chocolate in selected cities, 2004

% of chocolate consumers

	Weighted sample size ('000)	As snack	When work overtime	Serving guest	When hungry	As health supplement	Outing/ traveling	Others
Beijing	3,249	74.3	4.6	8.4	21.1	28.2	10.4	0.3
Shanghai	4,843	81.6	4.5	15.6	19.7	18.5	13.6	1.2
Guangzhou	1,501	80.6	4.7	14.3	11.7	20	10.1	0
Shenzhen	1,600	76	3.6	17.1	12.1	16.5	18.2	0.4
Chengdu	1,031	73.2	2.6	9.8	10.4	11.7	20.1	0.2
Chongqing	684	82.4	2.1	5.1	9.1	6.6	17.7	0.7
Wuhan	1,670	77.3	2.2	9.9	8.9	14.4	19.3	0.5
Xi'an	915	71.5	2.7	10.9	4.4	21.7	22.7	1.8
Shenyang	1,347	71.5	2.2	7.7	15.2	26.3	14.9	0.8
Nanjing	1,166	77.5	2.1	14.2	9.2	9.4	15.9	0.3

Source: IMI Consumer Behaviors & Lifestyles Yearbook 2004-2005

(iv) Foreign vs. Local chocolates brands

China's chocolate market can be broadly divided into three segments. Multinationals like Effem Food (Beijing) Ltd which owns the famous brands Dove, M&M's, Maltesers and Snickers; Shanghai Hershey Food which owns Hershey's and Hershey's Kisses; Ferrero China Ltd and Cadbury Food Co Beijing lead the way in the high-end segment. These products are generally of higher prices and the quality is considered much better. The mid-range segment mainly comprises of well-known domestic brands such as Le Conté of Shenzhen Le Conté Foodstuff Co Ltd and Shenfeng of Shanghai Shenfeng Food Co. Ltd. Their products are usually popular in big cities. The lower end market is also occupied by domestically produced chocolates, which are mainly sold in smaller cities and rural areas.

In recent years, consumers in China are showing a growing preference for foreign chocolate brands, although they cost a bit more – on average, foreign confectionery products are priced at approximately a 15% premium to local products. International brands have dominated the chocolate markets in major cities and captured over half of the market share.

Consumer tastes and preferences in the confectionery industry are fast-changing, so innovation and product improvement are important success factors. Foreign chocolates generally have a competitive edge in the market, due to their novel and unique flavors, shapes and packages. Foreign chocolate brands also offer more varieties than local brands. Most foreign chocolates are a blend of chocolate base, cereals, low-calories sweets, fruits or nuts. Cadbury chocolates, for example, come in a range of flavors and varieties. There are black chocolates, white chocolates, milk chocolates, chocolates with hazelnuts, coffee-, toffee- fruit jelly- fillings, etc. The foreign chocolates taste good and many of them also contain about 30-60% fewer calories, hence are popular among women. What's more, large chocolate manufacturers such as Kraft and Effem have invested in local manufacturing facilities. By using less expensive labor and avoiding high tariffs, their products become more affordable. These products are also often tailored-made to meet local market needs in terms of packaging, marketing and price.

In comparison, China's domestic chocolate products are characterized by low prices. If a box of Cadbury's goes for about 100 yuan, a same-sized Shenfeng – one of the most expensive local brands in China – goes for half of that. Only a few brands have established quality images. Most of them are generally less attractively packaged and less aggressively marketed due to budgetary constraints and limited experiences. Besides, many of the local players are also overshadowed in product quality. Local grinders mainly buy low-quality beans from Indonesia, which they process with butter and powder. Moreover, some domestic firms use cocoa butter substitutes, which are much cheaper. Many smaller companies even use discarded cocoa shells to replace actual beans. As commented by foreign consumers, Chinese brands of chocolates have a relatively lighter weight, leave people a greasy feeling in the mouth, and some even taste nothing like chocolates. Nonetheless, in recent years, domestic chocolate makers are expanding aggressively, at a faster pace than their foreign rivals. They have been putting more efforts in product development, technological upgrading as well as brand building. For instance, Shenzhen Le Conté Foodstuff Co Ltd has established its first R & D center in Shenzhen to strengthen its product development of confectionery and snacks. The gap between multinationals and their domestic counterparts is narrowing. The new standard on chocolate and chocolate production also puts pressure on domestic enterprises to upgrade their product standards. The ill-performed enterprises are likely to be forced out of the market. The market is expected to become more consolidated and achieve an overall upgrading.

(v) Market players and brand performance

According to CMMS, the top 5 brands in the chocolate market are Dove, Cadbury, Le Conté, Nestle and Hershey's. Dove of Effem Foods (Beijing) Co Ltd is the big winner, with half of the respondents cite it as the most frequently purchased brands. It is the number one brand in all major cities. Quality assurance, decent brand image and extensive marketing activities have contributed to the brand's strong position in the market. Dove has a full-range of products. It also launches new products regularly to create purchase desire. Furthermore, since 2002, Dove has been strengthening its promotion and product display in various retail stores and has achieved great success. It has its special promoters in supermarkets and hypermarkets to introduce Dove products to passers-bys. To stimulate impulsive purchase, Dove products are also displayed near cashiers in supermarkets and hypermarkets. Knowing that understanding consumer needs is a critical step to win the market, Effem Foods launched its online survey "Seven Reasons for Loving Chocolate" in one of the major websites in China www.sohu.com in early 2005. The first 100 participants who get correct answers were entitled to win Dove chocolates as prizes. It is reported that, with all these efforts, Dove began to turn loss to profit in 2004.

While foreign players dominate sales, only a few domestic chocolate brands are able to make a strong presence in the market. Le Conté is the most popular domestic brand for chocolates among all. It is said that Le Conté recorded a turnover of 650 million yuan, far ahead of its domestic counterparts. Le Conté has a diverse range of product offerings, from low-end to premium, from chocolate bars to boxed assortments. Recently, Le Conté has invested 200 million yuan into new product development in an attempt to satisfy the diversifying market demands. Le Conté's another key successful factor is its effective distribution system and well-established distribution network. It makes use of professional distributors rather than working with the retail stores directly. This strategy enables it to have quicker capital flow. Besides, its impressive image, as well as its exotic brand name, has created a very positive impression among Mainland consumers. Though, it is noteworthy that Le Conté consumers have lower purchasing power (monthly household income) than the top foreign brands consumers.

Appendix

Fresh food vs. Packaged food

Traditionally, Chinese consumers place great emphasis on the freshness of food and the majority of their food expenditure is spent on fresh food. Fresh food is particularly appealing to Chinese consumers not only for its cheaper prices compared with that of the packaged or processed food, but also for its health and nutritional value.

However, rapid urbanization has brought about considerable changes in food consumption habits. In urban cities, where the pace of life is becoming more hectic and a wide variety of packaged foods are available, consumers choose convenience over freshness to alleviate cooking burden. Besides, with the improvement in living standards, consumers in urban regions are becoming more hygiene-conscious, especially after the outbreak of mad cow disease, SARS and bird flu. They are shifting their consumption from loose unbranded food to more expensive packaged branded ones. The spread of supermarkets also provides easier access to packaged food and convenience food. Other important trends in the sector include the rapid increase in household ownership of refrigerators, freezers and microwave ovens, which has boosted sales of frozen and heat-and-eat products, such as lunch boxes, frozen congee and “dim sum”. On the other hand, to overcome Chinese consumers’ resistance to the consumption of packaged food, especially the frozen and canned ones, manufacturers have taken measures to improve the quality, safety standards and nutritional value of these products. Against this backdrop, sales of packaged food are improving in major Mainland cities.

Rural residents, however, less welcome packaged food. This is attributable to their tradition, lower income levels and the underdeveloped retail network in rural areas. The agricultural population tends to prefer fresh products to packaged food for their cheaper price, better taste and higher nutritional value. Low penetration of refrigerators and microwave ovens also hampers the sales of frozen food. Besides, the poor retail network and distribution inefficiencies in rural areas have driven up the retail prices of packaged food and thus many rural residents find packaged food products less affordable. However, as the government presses ahead with its plan to build a national retail network in the rural market through the “Market Project of Thousands of Villages and Townships” (萬村千鄉工程), the development of the rural retail market will be greatly facilitated, enabling the rural consumers to enjoy a wider array of products at lower prices. These will help boost packaged food consumption in the rural regions.

Exhibit 7 tries to summarize the key factors affecting urban and rural residents’ choice of fresh and packaged food.

Exhibit 7: Key factors affecting urban and rural residents’ choice of food

Urban

Fresh Food
- Freshness
- Higher nutritional value
- Better taste
- Cheaper price

- More hectic pace of life
- Rising income & living standard
- People are more hygiene- and health- conscious
- Wider choice of packaged food available
- The prevalence of supermarkets

Packaged Food
- Convenience
- More hygienic

Rural

Fresh Food
- Freshness
- Cheaper price
- Limited access to packaged food
- Low penetration of refrigerator or microwave oven
- Not used to consume packaged food, such as frozen food
- Higher nutritional value
- Better taste

China National Commercial Information Centre (CNCIC)

中華全國商業信息中心簡介

China National Commercial Information Centre, formerly under the Ministry of Internal Trade of PRC, is a reputable national statistics centre in commercial area. Authorized by the State, CNCIC is responsible for collecting, compiling, analyzing and releasing market data; and producing magazines, reports and numerous publications. One of the important functions of CNCIC is to provide support for the government officials and bodies in formulating macro-control policies in the commercial area.

CNCIC possesses a powerful database and data tracking system. Over 260 large-scale retail enterprises report their sales data and other detailed information to CNCIC every month. Apart from that, CNCIC also has special access to more than 5,000 commercial enterprises' yearly statistical and financial data.

With a wealth of market data, comprehensive coverage and well-developed information system, CNCIC is known for excellence in providing information-based solutions for enterprises, such as formulating strategic expansion plan and conducting marketing research on the Mainland.

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The Li & Fung Group is a Hong Kong-based multinational company consisting of three distinct core businesses: export trading, distribution and retailing. Founded in Guangzhou in 1906, Li & Fung Group, with an annual turnover exceeding US$8 billion, operates in some 40 countries and regions and employs over 18,000 people worldwide. One of its core competency is Supply Chain Management (SCM).

Li & Fung Research Centre ("the Centre") researches and publishes reports on wide-ranging topics: Chinese economy, consumer market, retail sector, trade-related issues, and FMCG industries, etc. Apart from providing internal consultancy for the Group and its clients, the Centre also participates in formulating business strategies in the Mainland market.

The Centre has been actively promoting the application of SCM. In 2003, the Centre published the book "*The Orchestrator of Global Supply Chain Management*", which is regarded as a very useful reference among businessmen and academics in the Chinese mainland, Taiwan and Hong Kong.