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Global Agricultural Information Network

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RETAIL FOOD SECTOR

Spending on Food Surges While Distribution Remains a Challenge

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Report Highlights:

In the four years ending in 2008, urban Chinese consumers increased their spending on food by an average of 17% per year. This is significantly faster than the impressive increase in the size of China's economy. The excellent quality and safety reputation of American food products has allowed U.S. exporters to benefit from this growth. While the Chinese economy has slowed this

year, it is still growing faster than any other major economy. This fact, and the Chinese customers taste for quality products, makes the Chinese market very attractive to many U.S. producers of food products.

Post:

Shanghai ATO

Executive Summary:

As Chinese consumers get richer, they are spending more money to diversify their diets. Consumption of meats has been increasing more rapidly than overall food expenditures and consumption of western style products is also growing. Rapid economic growth and a stronger Chinese yuan has caused the total U.S. dollar sales value of food and beverages to rise by 26.2% to \$132 billion in 2008.

Sales of most imported products have found their greatest success in hypermarkets and in specialty supermarkets. Some products, such as fresh fruit, frozen vegetables and nuts, have much deeper penetration, and some supermarkets and convenience stores may be becoming more interested in imported products.

International hypermarket retailers generally have a high level of familiarity with imported brands and products, and recognize the value of bringing new products to market. Hypermarkets frequently source high-volume merchandise directly from manufacturers but rarely do so with imports. Hypermarkets in China tend to develop groups of favored distributors. They dislike working with unfamiliar companies unless they can offer a large number of products, strong marketing support, or some other incentive.

Specialty supermarket stores include those targeted to expatriates, upscale and upper-middle Chinese consumers and shoppers that want organic foods, wine, cheese and similar high-end products. These stores have proliferated in recent years, not only in first tier cities such as Shanghai or Beijing but also in some second tier cities.

Retail distribution channels have not grown to match the number and quality of retail outlets. China does not have a nationwide network of trucks, highways and cold storage warehouses that can efficiently deliver supplies from the manufacturer or importer to the store shelf. A lack of appreciation for the value of maintaining the cold chain creates special problems for temperature sensitive items. With some notable exceptions, distribution is handled on a store-by-store or city-by-city basis, with stores receiving most imports through a local distributor, often even when alternatives exist. Because of their relative size, stores are able to effectively pass all market risk onto the distributor. Distributors, in turn, tend to be very conservative about new products.

Distribution varies widely throughout China based on geography, product type and retail sector. As a general rule, the three cities of Shanghai, Guangzhou and Beijing have the best infrastructure and the largest number of experienced distributors. Increasingly, those systems are being extended to the large webs of satellite cities surrounding Guangzhou and Shanghai. Other major cities along the eastern seaboard, beyond the reach of the 'big three,' generally have good logistics infrastructure,

but most still rely on one of the 'big three' as an entry point for imports. Farther inland, there are a number of large cities with good market potential. Logistics can be problematic, but improvements in the national highway system have made trucking direct from Shanghai or Guangzhou far easier than it was just a few years ago. As a result, high value and temperature sensitive products shipped by truck directly from the importer to a local distributor do surprisingly well. Currently, many secondary cities have only a single distributor for imports, particularly for high-value or temperature-sensitive products.

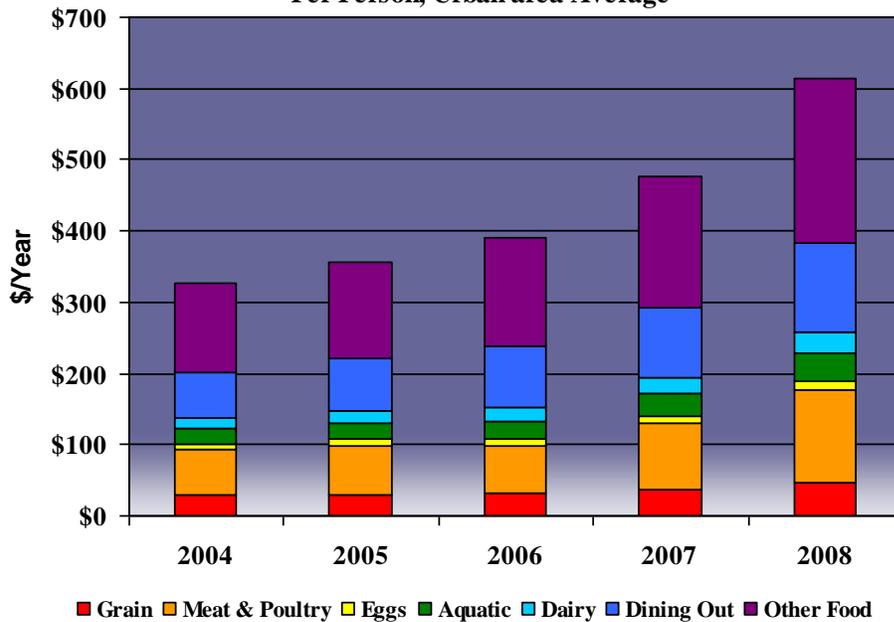
The most serious competition for U.S. food exporters comes from local and joint venture food producers and processors. The quality of fruit and vegetables in particular has increased rapidly, and many local traders now contend that the best of China's fruit is similar in quality to imports. The general trend to date has been for local manufacturers to push imports out of the price-driven mass market and into niche markets where quality and novelty are more important than price. The U.S. remains the largest single exporter of consumer-oriented food to China, and is the only exporter with a presence in most categories.

China is not a single market but a jigsaw puzzle of small, overlapping markets separated by geography, culture, cuisine, demographics and dialects. As such, there is no single formula for success in China. The fragmented distribution and logistics systems help to reinforce existing divisions. While smaller emerging cities are still relatively small consumer markets compared to Shanghai, Beijing, and Guangzhou, they are starting to grow faster than the major markets and many would be considered large cities in countries other than China.

Consumer Spending Patterns

As Chinese get richer they tend to spend much more money eating out and to diversify their diets. Consumption of meats has been increasing more rapidly than overall food expenditures, and consumption of western style products is also growing rapidly. Strong and continuous economic growth caused urban Chinese to increase their spending on food by almost 17% per year on average between 2004 and 2008 when measured in U.S. dollars. Expenditures on food almost doubled over that time period. While the growth rate has almost certainly been a little lower in 2009, it is probably still impressive.

Spending on Food in Urban Areas Per Person, Urban area Average



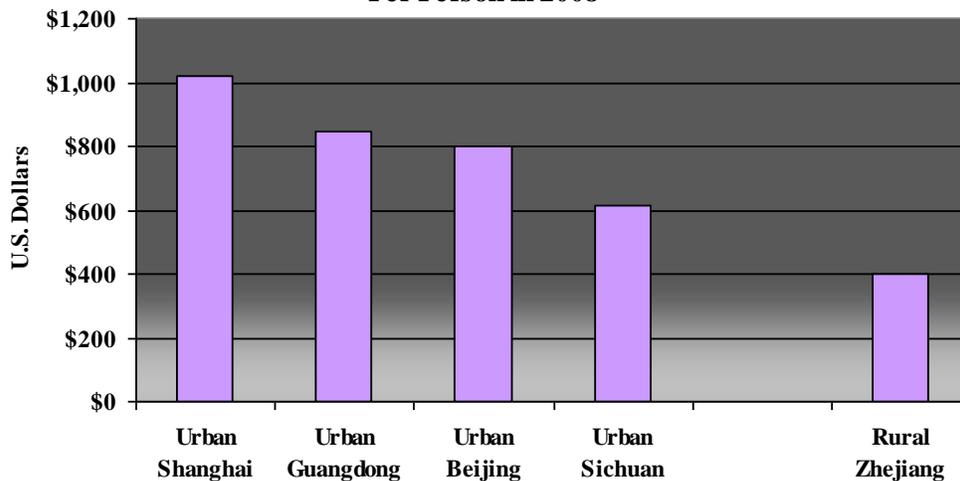
Source: China Statistical Yearbook 2009

While average annual food purchases for all cities was slightly more than \$600 per year, per person food consumption in Shanghai was slightly more than \$1,000 per person, and that in Beijing and Guangdong was about \$800 per person. This compares with U.S. food purchases per person of about \$2,300/year. Urban food purchases per person in Sichuan, a province in Western China that contains the city of Chengdu, come in at the national average for urban areas - demonstrating the potential of markets in western China. While there are some smaller cities where per capita income is about equal to that of Shanghai (such as Ningbo), the population and wealth of the three largest urban areas - Shanghai, Guangdong, and Beijing - lead most exporters to concentrate on at least one of those markets.

Even some of the wealthiest rural areas in China - those in the commercial province of Zhejiang south of Shanghai - have a lower level of consumption than urban areas in poor provinces. Disposable income in these areas is rising rapidly however. If the current consumption data is correct, the rural population in Zhejiang province may achieve Shanghai's current level of consumption in 15 years. The population in most urban areas will likely still be more wealthy.

Annual Purchases of Food in Selected Areas

Per Person in 2008



Source: China Statistical Yearbook, 2009

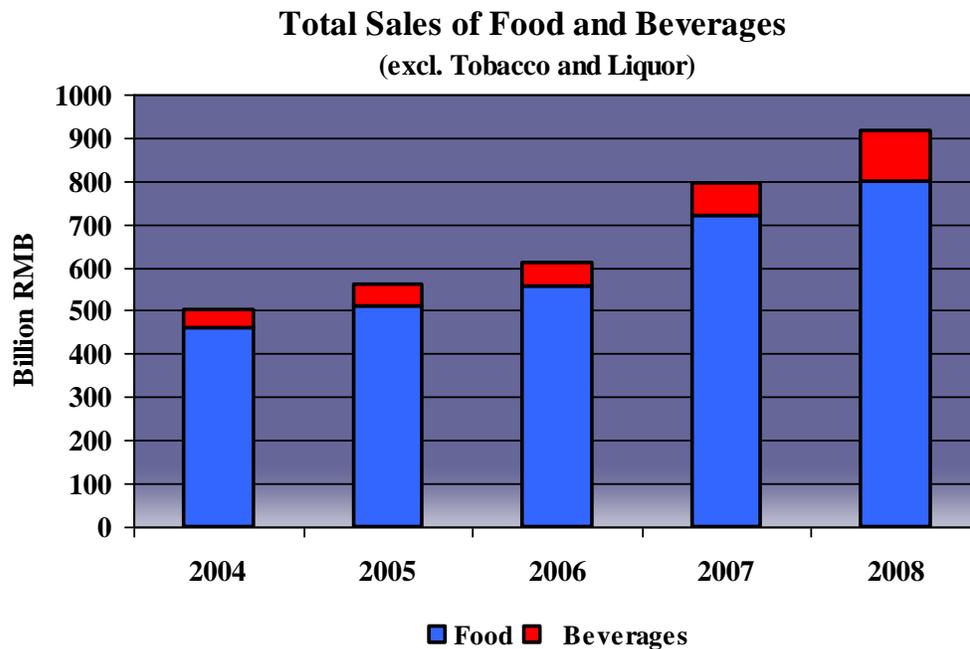
China is a very large country and different parts of China are at different levels of development. However, there are large variations of income and pockets of wealth in all large urban areas, and Chinese cities are no exception. The variation of wealth in China is illustrated in Table 1 in the Appendix. The wealthiest areas in China are Beijing and Tianjin in the north, Guangdong and Fujian in the south, and the Shanghai, Jiangsu, Zhejiang area in eastern China.

There are many urban centers in China that westerners have not heard of. Even a "small" city by Chinese standards may have millions of people. These are becoming much more prosperous, and their growth rates are starting to exceed those of the three large urban areas. It would be a mistake to overlook these markets and the potential to develop strong market positions in them. While there are certainly opportunities in these secondary markets, the number of distributors handling your type of product may be very limited. Given differences in regional tastes, logistical difficulties, and the size of China, many exporters choose to focus in a particular region of China first rather than try to develop the entire market at once.

Market Size and Segments

Determining the size and rate of growth of Chinese purchases of food and beverages is complicated. The official data does not attempt to pick up the smallest enterprises, and the usual concerns about data quality in a developing country are compounded by China's legacy of central planning. The Yuan also rose by about 9.5% against the U.S. dollar from 2007 to 2008. This

gives an added boost to Chinese expenditures when measured in dollar terms. According to China's 2009 Statistical Yearbook, the total sales value of food and beverages rose by 15.3% in 2008, from 793 billion RMB in 2007 to 914 billion RMB in 2008. If you are U.S. exporter, however, the change in U.S. dollars may be more useful to look at. Using average annual exchange rates, we find that the total sales volume in U.S. dollars rose by 26.2% in 2008, from \$104 billion in 2007 to \$132 billion in 2008.



Source: China Statistical Yearbook 2009

Market Segments

While 2008 sales data for the major retailers is available, it is of limited use when discussing market segments. This is because retailers in China often cross several market segments. Some domestic players have hypermarkets, supermarkets, convenience stores, and specialty stores. However, we can say that most imported products have found their greatest success in the hypermarkets and in specialty supermarkets. Some products, such as fruits and snacks, have much deeper penetration, and some supermarkets and convenience stores may be becoming more interested in imported products.

Hypermarkets: The hypermarket format is much more concentrated than other grocery channels. While some domestic retailers (including CRV and Lianhua) have a significant presence, this

format is dominated by foreign operators including Carrefour, Wal-Mart, Metro, Auchan and Tesco. In Shanghai for example, the 82 foreign hypermarkets accounted for 78.6% of the total hypermarket sales volume in 2008. Other retail channels, most notably supermarkets, are highly fragmented and controlled by domestic players.

Multinational chains such as Carrefour and Wal-Mart benefit from their reputation for offering better quality products than most domestic retailers, thanks to stricter quality control in a country where food safety is a major concern after several disturbing food scandals in recent years. In food products, especially fresh food, hypermarket retailers benefit from better hygiene controls and a higher volume flow rate, and are thus able to ensure better food safety for consumers. As such, an increasing number of Chinese consumers visit hypermarkets instead of independent food stores for grocery shopping. Fresh produce has become an attractive section to draw in Chinese consumers.

International retailers generally have a higher level of familiarity with imported brands and products, and recognize the value of bringing new products to market and promoting them. Hypermarkets are also the major sales venue for imported food products, due to international retailer's familiarity with imported products and better management and organizing skills. Most are experienced in promoting new products, and flagship stores like Carrefour's Gubei store or Lotus' Superbrand Mall store in the Pudong area have it down to a science. Despite this, imports rarely constitute more than 5% of total SKUs even in high profile stores. Nevertheless hypermarkets are the single best retail venue for imported products.

Most hypermarket chains vary the proportion of imported goods they carry in individual stores depending on the income level and foreign population that the store serves.

For the time being, hypermarkets are still mostly limited in first and second-tier cities because of lower rural incomes. Until wealth spreads more deeply into rural areas and infrastructure improves, most places outside the first and second tier will not have access to modern retail formats.

The hypermarket has been well accepted by affluent customers due to large parking facilities, monopoly stores and numerous restaurants and coffee shops that enable consumers to combine shopping and leisure activities. Most hypermarkets in China offer free shuttle bus service to nearby communities and constantly offer promotional items to attract consumers. These measures successfully draw heavy traffic to the store, but some consumers go to the store to buy the promotional items only, reducing the purchase per customer. This active promoting may also drive away some high-end consumers who desire a less crowded environment and more concentrated product display. As a result, specialty supermarket stores such as City Shop in Shanghai and Wuhan

Life & Theatre supermarkets, both targeting high and upper-middle class clients, have successfully attracted customers from the hypermarkets.

The most decisive component in hypermarket food promotion for imported goods is free sampling. Consumers are cautious rather than impulsive buyers, and will rarely spend money on a product they have not had a chance to try. Hypermarket promotions also come with many strings attached. Some charge listing fees, most demand that promoters be provided at the distributor's expense (some even charge fees to have the promoters on their premises). Some require two months' credit, while others pay up front. Other conditions include accepting returns of unsold products at the end of the promotion. Although these problems are usually handled by the distributor, they will affect your sales.

In addition to the major chains, hypermarkets often face competition (especially in Northeast and Central China) from local department store operators with one or two locations and specialty supermarket stores. Department stores have evolved in the direction of hypermarkets, adding large food stores, while many hypermarkets have taken on some attributes of department stores.

Hypermarkets in China tend to be somewhat smaller than their western counterparts, and very few (excepting Metro) follow the big-box format faithfully. In large cities, they are typically multi-story operations. Most act as small shopping malls, setting aside a large amount of space for independent boutiques and eateries, a habit that tends to reinforce the perception of hypermarkets as places for occasional shopping expeditions rather than daily shopping. For the hypermarket itself, the food sales area typically accounts for about half of the total area.

Management within the stores tends to be quite good, but distribution has not kept pace. Hypermarkets in China tend to develop groups of favored distributors. They dislike working with unfamiliar companies unless they can offer a large number of SKUs, strong marketing support or some other incentive. Distributors tend to be very conservative in introducing new products, due to the high level of market risk. As a result, exporters with a limited product range need to work both ends of the problem at the same time: identifying a retailer that is interested in the product, and identifying a distributor that either has an existing relationship or is willing to work with the retailer.

Supermarkets: Imported food is relatively rare in Chinese supermarkets. Products that do well in this sector tend to be commodity products already widely available, such as fresh fruit, frozen vegetables and nuts. Supermarkets rarely if ever import directly, or even buy directly from an importer, tending instead to rely on wholesale markets and local manufacturers or distributors.

Stores with a significant expatriate community nearby are likely to carry imported breakfast cereals and a perfunctory selection of imported sauces (especially pasta sauce) and seasonings. The best possibilities are in the smaller, privately held chains, which are more likely to see the value of high-margin imports and tend to have better integrated distribution systems. Such chains may carry products as varied as wine, exotic fruit (avocados, in one case) or confectionery, but only in low volumes. Even so, price will remain a consideration. State-owned supermarket chains generally have less integrated management and distribution. Opportunities exist, but only on a limited basis with a small number of stores, and only for products already present in the market. For either state-owned or private supermarkets, direct contact with company managers is the best means of introducing a new product.

Import penetration is lower in supermarkets than other modern retail venues. U.S. food products in these venues are typically limited to frozen corn and mixed vegetables, frozen potato products, some packaged goods and occasionally fruit (apples or oranges). Other items tend to appear on a haphazard basis: past checks have turned up breakfast cereals, low-end wines and Washington state apples. The sparse selection of imports is rooted in the customer base of these stores, which focus on working class shoppers, who are notoriously price sensitive and less inclined to try new products than the more well-heeled customers that frequent hypermarkets and upscale convenience stores. Distribution is also a problem, as stores tend to source from local distributors, directly from manufacturers, or from local wholesale markets. Supermarkets are often franchised in China and can have much smaller footprints than is common in the United States.

In order to compete with hypermarkets, Shanghai's supermarkets are putting more efforts into enlarging their fresh section, catering to the tastes and demands of local consumers. The local government is also encouraging supermarket chains to create 'fresh' supermarkets, expanding the floor space dedicated to fresh products from less than 1/3 to over 1/2. Over 300 stores in Shanghai have finished the change. And sales of fresh produce are gradually increasing. Supermarkets throughout the region (including Suguo, a unit of CRV) appear to be moving in this direction, but are being slowed by problems in sourcing large quantities of quality product.

Specialty Supermarket Stores and Boutique stores: These stores have multiplied in the last few years. They are often located adjacent to high-end department stores or upscale business centers. Built to attract upscale consumers in first and second-tier cities, they have a high proportion of imported food products – ranging from 10 to 80 percent of products. They are not only present in first tier cities such as Shanghai but also in some second tier cities like Wuhan.

Some high-end and specialty products first enter the Chinese market through these types of outlets before moving on to larger venues. Some of these companies also include import/distribution operations, and can assist exporters with issues such as labeling and product registration. Otherwise, exporters will need to identify a good distributor. In the case of high-end and specialty products, HRI-focused distributors (who are familiar with the products but may lack experience with labeling issues) may be as helpful as larger retail-oriented distributors (who often lack experience marketing high-end products), particularly in emerging city markets. Because of the small scale and highly varied nature of this market segment, interested exporters should contact the relevant ATO for a list of potential venues.

In Shanghai, City Shop Supermarket continues to be one of the best single venues for imported food, and now does significant business as a distributor of imports to other stores. Hong Kong based City-Super and CRV's Ole may be planning to enter the Shanghai market in the near future.

The leading boutique retailers in northern China are BHG (Beijing Hualian Supermarket) and Ole in Beijing, Hisnese Plaza in Qingdao and Jin Bou Da in Zhengzhou. Specialized imported food supermarkets also target high-end customers and expatriates in Beijing, Qingdao and Zhengzhou. BHG is also opening stores in Nanjing.

Convenience Stores: Management in convenience store chains is probably the best of any retail sector. All stores have refrigerator and freezer sections, microwave ovens, and most have a selection of hot snacks (mostly meatball or tofu on skewers). Store layouts are highly standardized, although some chains have developed more complex systems that customize product selection to the peculiar location based on past sales patterns.

The concept of trading higher prices for convenience will take time to be accepted by more consumers. Competition also tends to make convenience stores conservative about pricing, though ATO Shanghai's experience indicates that chain managers are more price sensitive than their customers.

The convenience store sector is expected to expand dramatically as consumers look to reduce time in meal preparation. Stores compete aggressively for good locations, and it is not uncommon to see three different convenience stores within 100 feet of each other in prime areas.

Import penetration in this sector tends to be relatively low, despite a high level of interest on the

part of several chains. Being largely domestic companies, management at convenience store chains tends to be less familiar with imported products than their counterparts in the hypermarket sector. A second difficulty faced by imports is packaging: convenience stores typically require smaller package sizes, being focused mainly on single-serving products. Exporters are advised to open discussions directly with chain officials to identify products with potential, and ensure that packaging meets their needs.

Then the exporter will need to identify a local distributor that can handle the import paperwork and labeling issues. One alternative to this is to work with an importer/repacker, who can import in bulk, then package the products in China with Chinese labels and packaging appropriate to the convenience market. This strategy has proven extremely successful for U.S. prunes.

Managing logistics for convenience stores is very challenging. Limited shelf and storage spaces make convenience stores heavily reliant on sophisticated logistic systems that should provide delivery 2 or 3 times a day. But in Shanghai most convenience stores are guaranteed just one delivery per day. This adversely affects the ability of these stores to offer the fresh and ready-to-eat products that are among their most attractive offerings. In addition, the need for small package sizes limits their set of suppliers.

Some hypermarket operators in first and second-tier cities are expanding their small-format convenience stores to increase market share and better utilize existing supply channels. Most are located near upscale communities and business centers and target white-collar workers, upper-middle class and young consumers in search of convenience. The stores feature daily necessities and ready-to-eat items.

The world's largest convenience store chain, 7-Eleven, which opened its first store in Beijing in 2004, now has 70 outlets. The company sees profits increasing during the economic downturn given a growing number of consumers buying food at stores instead of eating out.

Ferocious competition has spurred efforts to innovate and to target niche markets. Quik and Kedi, the two leading convenience stores in Shanghai, have both entered into deals with gas station operators to open markets in their stations. Lawson's pioneered efforts to target white collar employees and service staff in shopping districts with high-quality Japanese style lunch boxes. Kedi also offers lunch boxes, which are quite popular among office workers in the central business areas. Family Mart expects to benefit from superior management and technology (they may be surprised by the local competition). Nearly all convenience stores offer a range of services to draw foot traffic, with Alldays ushering the latest innovation by providing China Life travel insurance policies at their stores.

Shanghai's convenience store industry is by far the most developed in the country, with the city playing home to an estimated 5,650 convenience stores—nearly 1/3 of the national total. One source estimates the number at 1 store per 4,400 residents (not including immigrant workers), comparable to saturation levels in Japan and the U.S. Despite this, the sector continues to grow.

Shanghai's convenience sector is overwhelmingly dominated by subsidiaries of the giant state owned supermarket chains: Quick (Lianhua), Alldays (Nonggongshang), Kedi (Nonggongshang via its Bright Dairy subsidiary), with only a few foreign players such as 7-Eleven and Lawsons (Lawsons was a JV between Hualian and Lawsons Japan, but Lawson Japan may have sold its shares back to Hualian). Japan's Family Mart entered the city two years ago, and now has 126 stores in Shanghai.

Traditional Markets: These continue to be a presence throughout China, although they are no longer the dominant factor in the larger cities. Traditional markets fall into three general categories: wet markets, variety stores (xiaomaibu), and fruit stands. Wet markets specialize mainly in fresh vegetables, meat, poultry (sold live), eggs, tofu and to a lesser extent, fruit and staple foods. Sanitary standards are extremely low, particularly for meat. Officials generally regard wet markets as an eyesore, as well as a source of both food safety problems and unregulated (i.e., untaxed) commerce. The SARS epidemic of 2003, followed shortly by avian influenza outbreaks, provided more impetus to efforts to reform or close these markets. Nonetheless, they persist. The main reason for this is a lack of alternatives for buying fresh vegetables and, to a lesser extent, meat. With local government support, however, supermarkets' efforts to expand the fresh section, and especially with consumers' growing concerns over food safety, these traditional markets will gradually be phased out.

The other traditional formats are small variety stores (xiaomaibu) and fruit stands. The typical xiaomaibu is much smaller than even a convenience store, family owned, and stocks an eclectic mix of products. Although they face a serious challenge from convenience stores, the xiaomaibu persists even in Shanghai. While convenience chains follow standard formats and target key sites (train and bus stations, schools, hospitals, etc.), xiaomaibu are infinitely adaptable. Small size and independent ownership allows these shops to adapt to individual sites such as apartment complexes, and adapt their product selection even to match individual consumers. Like convenience stores, xiaomaibu also offer a range of services such as bill payment and IP telecommunication card sales.

Fruit stands fill another gap left by the convenience stores, which rarely carry more than one or two

types of fruit. Sales are boosted by the tradition of giving gifts when visiting friends, and most fruit stands will wrap fruit baskets to order. Fruit stands frequently carry imported fruit, usually for inclusion in fruit baskets. However, they are generally regarded as poor venues for imported products, as they are generally price driven, poorly regulated and lack the means to store fruit properly. Counterfeiting is widespread in these markets, and where a brand name adds value, it is certain to be copied. As a result, there is little room for marketing and promotion of imported products. While both xiaomaibus and fruit stands will likely continue to decline in numbers relative to convenience stores, China's high urban population densities are likely to support their continued existence for many years.

Product Distribution

Retail distribution channels have not grown to match the number and quality of retail outlets. Roughly the size of the continental U.S., China does not have a nationwide network of trucks, highways and cold storage warehouses that can efficiently deliver supplies from the manufacturer or importer to the store shelf. With some notable exceptions, distribution is handled on a store-by-store or city-by-city basis, with stores receiving most imports through a local distributor, often even when alternatives exist.

Because of their relative size, stores are able to negotiate highly favorable terms that include free return of unsold products, high listing fees for new products, and credit terms, effectively passing all market risk onto the distributor. This gives store managers a powerful incentive to favor the local distributor over alternatives that offer less generous terms. In at least one case, an international retailer's effort to establish single-desk distribution of imports failed when their own stores refused to work with the selected distributor.

A second reason for reliance on local distributors is the tendency of international retailers to expand rapidly nationwide rather than focusing on a single city or region, creating large numbers of isolated stores that lack the volume to support a dedicated distribution network. A final reason has to do with the role of relationships in Chinese business: local distributors can provide a store with a network of business and government contacts that are useful in resolving problems with minimal fuss.

Fragmentation among suppliers of locally sourced products, particularly of vegetables and meat, helps to perpetuate the dominant role of the local distributor. This is changing slowly, as the government encourages direct sourcing and farmers' professional associations become more

common, giving producers the ability to supply larger quantities from a single source and at a more consistent level of quality.

International retailers have recognized the problem and put a greater effort into improving the logistics system. Right now, Wal-Mart is focusing on building a nationwide distribution network, and has a recently built distribution center in Tianjin. The German retailer Metro has a centralized distribution system for many imported products, and a few large distributors have negotiated more favorable terms with retail chains at the national level, in some cases waiving listing fees. Carrefour also contracted with a third party logistics company to handle most of its imported grocery items. But fresh and frozen items still rely on importers or distributors to deliver to the stores themselves. The role of the local distributor in handling imports is declining. Nonetheless, for now, distribution remains the key obstacle to sales of imported processed foods in China's retail sector.

Because of the high level of risk they are expected to absorb, distributors tend to be very conservative about new products, particularly imports. As a result, penetration of imported foods into the retail sector is low. Even in relatively affluent cities, international retailers typically carry less than 1% imported SKUs. Notable exceptions include stores in Shanghai, Beijing, Guangzhou and nearby boomtowns, which are home to both large expatriate communities and to a large number of Chinese with overseas experience. Products that are already in the market but being sold mainly through gray channels or sub-distributors tend to be the most attractive to distributors.

Farther inland, distribution problems are complicated by China's heavily fragmented logistics systems, which make it difficult to transport products directly from the coast to deep inland cities. One survey in Chengdu found that temperature sensitive items, such as imported poultry and meat, changed ownership as many as five times before reaching the final user.

A lack of appreciation for the value of maintaining the cold chain creates special problems for temperature sensitive items. Even if cold storage is used at the port of entry and the retailer maintains the appropriate environment, getting drivers to maintain the correct temperature during transportation has proved difficult. While this certainly true in secondary markets, where frozen products often have a frosty covering, is also true in the major costal markets.

Distributors generally fall into one of two categories. The largest distributors tend to have longstanding relationships with the major retail chains, and can source in larger volumes and place products in a larger number of stores. However, they also tend to carry a large number of SKUs, and cannot dedicate resources to marketing any one particular item. Specialty distributors tend to

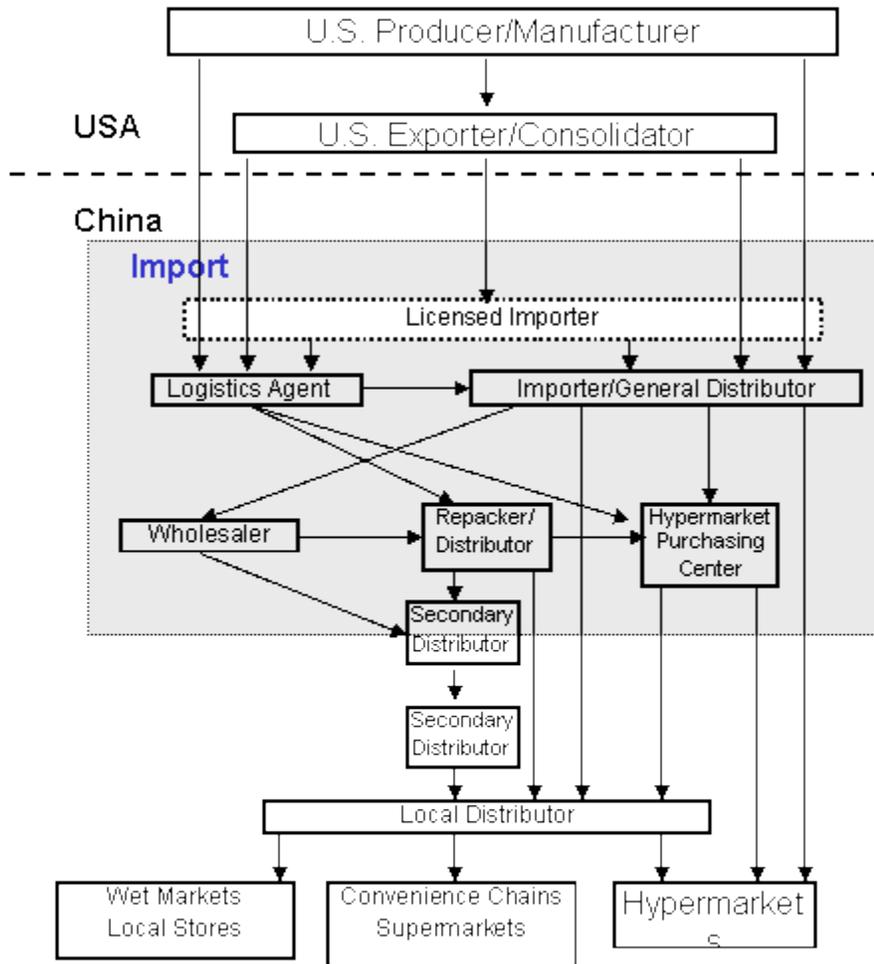
be focused on one area or product type. Although they sometimes lack the volume and connections of larger distributors, they tend to be more aggressive in marketing products and better at identifying and selling into specific niches. The quality of these smaller distributors varies widely, however, and exporters need to be very careful in selecting a partner.

A handful of retailers also act as distributors. Although they tend to provide less marketing support, they can be an effective means of getting product to retailers that have already expressed an interest, but cannot handle the import formalities themselves.

Geographic Differences in Distribution

Distribution varies widely throughout China based on geography, product type and retail sector. As a general rule, the three cities of Shanghai, Guangzhou and Beijing have the best infrastructure and the largest number of experienced distributors. Increasingly, those systems are being extended to the large webs of satellite cities surrounding Guangzhou

Chinese Distribution Channels



Source: ATO/Shanghai research

and Shanghai. Ports in these cities offer a growing array of services, including bonded storage (with temperature controlled facilities, if needed) and online inventory tracking. Some have duty-free industrial zones where products can be repackaged or further processed, with duty paid only on the original import value, and only after products leave the zone.

Other major cities along the eastern seaboard, beyond the reach of the ‘big three,’ generally have good logistics infrastructure, but most still rely on one of the ‘big three’ as an entry point for imports. The number of distributors handling imported products in these cities is usually limited. These tend to be good markets for commodity products such as meat, poultry, fruit and seafood, as well as sauces, condiments and wine.

Farther inland, there are a number of large cities with good market potential. Logistics can be problematic, but improvements in the national highway system have made trucking direct from Shanghai or Guangzhou far easier than it was just a few years ago. As a result, high value and

sensitive products shipped by truck directly from the importer to a local distributor do surprisingly well, while lower value and shelf-stable products that ship on local roads through conventional distribution chains face more difficulties. Distribution in these cities is generally underdeveloped. Many cities have only a single distributor for imports, particularly high-value or temperature-sensitive products. Products going through conventional distribution channels typically change hands numerous times before reaching their final destination. Distribution channels for HRI tend to be better developed, and may be the best place to start for exporters seeking to develop new markets.

Distribution by Product Type

Distribution also varies widely by product type. Channels for shelf-stable grocery products tend to be the most heavily fragmented and the most dependent on the good graces of local distributors. This is partly because market risk is perceived to be higher: although shelf stable, the number of SKUs tends to be high and turnover low compared to other product categories. Hence the risk that a product will not sell (and the distributor will have to accept a return) is higher. Meat, poultry and seafood also face fragmented distribution, but the combined demand from HRI and retail venues is sufficient to warrant special arrangements for these high-value products. Fresh fruit appears to have the best distribution, working through a patchwork of wholesale markets and specialized distributors that works better than it should. Imported frozen corn and mixed vegetables are almost universally available, reinforcing the notion that the problem is less one of logistics than of distribution. Wine deserves special mention, due to the presence of a community of specialized distributors, some of whom act as exporter, importer and distributor all in one, taking product directly to retailers.

New Trends in Retail

Direct sourcing of food and agricultural products from farm cooperatives has been adopted by most retailers in Shanghai and is growing elsewhere. This allows retailers to address consumers' concerns about food safety, reduce cost, and possibly improve product quality. On the imported product side, Wal-Mart started to directly source and import U.S. cherries this year.

Neighborhood Supermarkets were opened in Shanghai by Carrefour and Tesco this year. These outlets offer low prices and fresh food as their selling points. The prices in Tesco Express are as competitive as in Tesco Hymall (hypermarket). Seventy to eighty percent of the products in Carrefour's trial express neighborhood outlet are also fresh and live food. Making use of Carrefour's purchase and logistics system, its operating cost is much lower. Fresh and live products have become hypermarket's core products and are increasingly important to their sales. These

express outlets may turn out to be a way for supermarket to survive the fierce competition from hypermarkets and convenience stores. Such outlets can better cater to consumers' daily needs due to their convenient location. Shanghai Lotus opened a **neighborhood hypermarket** in 2008 which also has fresh food as its core offer.

Private label products are new development in China. Each hypermarket, supermarket and convenience store chain in China has a unique private label offer: Carrefour, Great Value, IKA, Tesco and Lianhua are private label lines from leading players. In terms of imports, more private label products are coming on the market here. Metro has moved ahead of the pack in this regard - it imports salmon from Norway by itself, and then packs it and sells in under its private label brand IKA.

Carrefour's Dia **discount stores** carry many of the same staple goods as supermarkets at discounts, but do not carry fresh products. Import penetration is also very low. While the threat from Dia and Nonggongshang's 5 Reminbi discount stores should not be understated, the concept has not succeeded thus far. The stores are small, carrying a limited range of products, and most of them are located nearby residential areas. The proportion of private label products in the stores is too small however, and some of Dia's products apparently did not appeal to Chinese consumers. The number of 5 Reminbi stores has fallen over the last few years as the concept struggles.

Several **specialty wine retail** outlets have opened in Shanghai. These sell a selection of imported and domestic wines and are not to be confused with state-owned liquor and tobacco stores. The most notable is Napa Reserve, which features a wide range of wines from that region of California. (Please see [CH8802](#) Shanghai_Retail Wine Show.) The Chinese wine market is more completely analyzed in the National Wine Market Report [CH9808](#).

Retailer Profiles

Domestic retailers generally have an advantage over foreign retailers, and China is not an exception to the rule. Lianhua and the Suguo - Vanguard combination are easily the largest food retailers in China. The three largest multinational chains - RT Mart, Carrefour, and Wal-Mart - have not been in a position to challenge the local incumbents for sales leadership. If you look at the hypermarket channel, or imported products however, the situation is different. Most of the Chinese domestic retailers focus on a clientele that is more representative of the Chinese population than that of the multinational retailers. They also have store base that is often older, partly franchised, and has large numbers of smaller properties.

While the domestic retailers are becoming more interested in imported products, importers have traditionally focused on, and gotten better results from, the multinational hypermarket retailers. The number of hypermarkets by retailer in selected cities and the total number of stores by retailer in Shanghai are presented in the appendix.

The table below gives a snapshot of the relative competitive position of some of China's leading food retailers. The data is for the year ending December 31, 2008. Much has changed since then. Wal-Mart now has more stores than Carrefour, and RT Mart and Auchan seem to be joining forces. The numbers in the following profiles reflect our current understanding.

Leading Food Retailers in China: 2008				
Company	Ownership	Business Line	Stores	Sales* ¥ billion
Chinese				
Lianhua	China SOE**	Super/Hypermarket/ Convenience	3932	74.0
Wumart	China Pvt	Supermarket/ Convenience	726	31.0
Suguo (CRV)	China SOE***	Supermarket/ Convenience	1802	45.0
Nonggongshang	China SOE	Super/Hypermarket/ Convenience	3330	39.0
Vanguard (CRV)	China SOE	Super/Hypermarket/ Convenience	2698	49.1
Xiuyijia (A. Best)	China Pvt	Department	105	25.0
Wuhan Zhongbai	China SOE	Super/Hypermarket	626	16.0
Multinational				
RT Mart	Taiwan	Hypermarket	101	49.4
Carrefour	France	Hypermarket	134	49.7
Wal-Mart	U.S. JV	Hypermarket	123	41.0
Metro	Germany JV	Hypermarket	38	18.5
Tesco	U.K. JV	Hypermarket	61	19.9
Auchan	France	Hypermarket	31	11.9
Lotus	Thailand	Hypermarket/Convenience	76	19.1
* Food and non-food sales			<i>Source: China Chain Store &</i>	
** SOE= State-Owned Enterprise			<i>Franchise Association 2008</i>	
*** Joint venture with China Resources Vanguard				

Hypermarkets

Wal-Mart's presence in China not only includes its Wal-Mart hypermarkets, but **Sam's Club**, and **Trust Mart**. Wal-Mart purchased 35% of Taiwanese owned Trust Mart in 2007, significantly expanding its footprint. *Trust-Mart* would be one of the biggest retailers in China even without its connection to Wal-Mart. This Taiwanese company has over 100 hypermarkets, mostly in eastern and southern China. While Wal-Mart has the option to purchase the remainder of Trust Mart in 2010, recent press reports indicate that Wal-Mart has suspended the merger. However, these reports may reflect negotiations about price by another means. Wal-Mart itself currently has 172 stores in China.

Compared to the other international retailers Wal-Mart may be more willing to open stores in secondary cities and in suburbs rather than directly targeting the higher income central city areas directly. Until recently, Wal-Mart's development in China had been mostly limited to the southeastern seaboard area where household consumption is high. In 2005, Wal-Mart made an entrance into Shanghai with the opening of a large suburban outlet. It has established a second company in Eastern China to manage its expansion in the Shanghai area. Wal-Mart set up its headquarters and opened its first store in Shenzhen in Southern China 13 years ago. Its "Everyday Low-Price" strategy helps Wal-Mart attract traffic, and it continues to aggressively open new stores to penetrate mainland second- and third-tier cities.

In addition to *Wal-Mart* supercenters, *Sam's Club* has gained a good reputation in introducing imported food to local consumers. To date, four *Sam's Clubs* have opened, including one in Shenzhen, one in Panyu, Guangzhou, one in Beijing, and another in Fuzhou. The Shenzhen store is reported to be one of the most profitable *Sam's Club* stores in the world. ATO/Guangzhou, along with several cooperators, is working closely with three *Sam's Clubs* in South China to conduct a regional promotion featuring various snack foods and fresh items.

Carrefour has made great efforts to increase its fresh produce SKUs to the range 3,000 to 5,000 per store. Carrefour currently operates about 156 stores in China, extending even to the far western city of Urumqi. Many of the new stores are or will be located in markets where Carrefour previously lacked a presence. Carrefour's recent overall strategy has been to increase investment and expand into more second tier and or third cities in China, mainly because of an increasingly saturated environment for retail outlets, and rising rental and manpower costs in first tier cities.

While Carrefour continues to dominate at the high end, with 19 hypermarkets presently in Shanghai alone, its single store sales were surpassed by Taiwan-based retailer RT-Mart and Wal-mart now has more stores.

Carrefour China has a new CEO with a finance background. Since his arrival, Carrefour has paid more attention to profitability and has become more conservative in terms of new product sourcing and merchandising. This impacts the introduction of new imported products. Carrefour's internal organizational structure and policy has changed to favor people with a finance background and a volume sales-oriented strategy.

RT-Mart had 102 stores in China, with 10 outlets in Shanghai alone, at the end of 2008. Although overall store numbers lags behind Wal-mart and Carrefour, its single store sales are the highest. It has reached an agreement with French retailer Auchan to set up a joint share-holding company listed in Hong Kong in the near future. Its goal is to pass Carrefour to become the largest sales volume retailer in China.

Auchan has stores in Shanghai, Beijing, and Chengdu. Its customers are largely upper-middle and middle class consumers. Auchan has a centralized system for import distribution. Its purchasing and distribution department are located in Shanghai.

Lotus has a target of 100 stores in the next few years. It has quietly expanded and has 21 stores in Shanghai, although turnover for these stores is lower than for Carrefour stores. Import products have a relatively small presence in its stores compared with the other retailers. And it has changed its marketing slogan from "Everyday Low Price" to "Freshen Your Life", indicating an attempt to stand out from its mass positioning. In terms of imports, it prefers to source directly for any volume-sales products on a consignment basis, which is relatively harder for U.S. exporters to accept.

AEON-Jusco is a key retailer in Northern and Southern China. It uses a Japanese General Merchandise Store (GMS) approach where the store sells many types of merchandise, including food, fashion, house ware and electronic appliances. AEON Jusco stores have an excellent reputation in southern China for carrying high quality imported foods. Their target customers are mid-to-high income consumers. *Jusco* stores encourage a wide variety of food categories and also cater to the expatriate community in the Pearl River Delta. Store managers in Southern China have been very eager to carry U.S. food and beverage products to meet the demands of their customers. Customer traffic in Shenzhen stores typically exceeds 20,000 shoppers per day. During the past three year, Jusco worked with the *ATO Guangzhou* office to hold American Food Festivals in its

Guangdong supermarkets. Each year the sales of U.S. food item increased by 20-30 percent.

In Northern China Jusco opened its first hypermarket in Qingdao in 1998, with 40,000 square meters of retail space and parking for 1,000 cars. The format links shopping with leisure by offering a supermarket, coffee shops, other shopping and restaurants under one roof, and became a top expatriate and middle class Chinese consumer destination. Imported food products account for 6 percent of total food products offered at Jusco and focus on fruit, snack food, beverages and dairy products. Jusco opened a hypermarket in Beijing last year just outside the Fifth Ring Road targeted at high-end consumers from surrounding upscale communities, and auto owners shopping on the weekend. In 2009, the retailer also moved into the convenience store business and currently operates nine convenience stores -- with plans to have 50 by the end of the year.

Metro relies on its niche-market strategy of targeting small and medium sized restaurants, effectively positioning itself as an HRI wholesaler and distancing itself from its competitors. To this end, Metro has added a training kitchen to its facilities in Shanghai. Historically it has opened stores more slowly than other international retailers, but it recently announced plans to open stores at much more aggressive pace. Depending on the opening dates of 4 new stores, Metro may currently have 42 stores throughout China.

Metro has the widest selection of imported products of any of the key retailers, and 10 percent of their sales revenue is from imported products. Metro has a membership system similar to that of Sam's Club or Costco. Their large section of frozen processed foods, including desserts, frozen vegetable mixes, and frozen potato products, is easy to use and open to U.S. products. Metro's main competition is the local wholesale market, not other high-end hypermarkets.

Its import company previously intended to import volume-sales products directly, but now more focuses on importing its own private label products from Europe. Its import department has been dismantled, and the staff has been re-allocated to product categories departments.

Tesco moved its headquarters to Shanghai in 2009 and has 19 stores in metro Shanghai. It opened a new retailing format in Shanghai in 2008. Called the "Express", it has fresh food as its core offer. Import products SKUs are relatively higher at Tesco than Lotus, but Tesco still lags behind Carrefour.

China Resources Vanguard (CRV) is one of the leading retail chain operators in China. This HK based operator manages hypermarkets, supercenters and superstores under the *Vanguard* brand

name. Its first store was opened in Hong Kong in 1984, and it entered the supermarket business in Shenzhen in 1991, Suzhou in 1995 and Beijing in 1998. Acquisition helped *CR Vanguard* become national number one retailer in terms of number of outlets and total sales. It acquired “*Suguo*” supermarket in 2004, and then purchased Tianjin “*Yuetan*” in 2005 and “*Jia shijie*” in 2007. In 2008, CRV completed the acquisition of “*Aijia*” supermarket in Xian. This year, CRV entered Wuxi by acquiring 100 percent stake of “*Yongan*” supermarket.

By the end of 2008, CRV had 2,700 stores (up 248 from 2007 figure) in China. This includes 200 hypermarkets and 2,306 supermarkets as well as over 80 community stores and 12 *Ole* stores. The total sales reached US\$9.4 billion. Generally speaking, *Vanguard* targets customers likely to buy local produce; however increasingly, higher income shoppers are beginning to show interest in high-quality U.S. imported foods. In some selected stores, special imported food section has been opened to promote imported food items. *Ole* stores are discussed further in the Specialty Supermarket section below.

Century Lianhua is the hypermarket brand of the state owned Balian group. This group’s food retail side is dominated by supermarkets, but it has substantial number of hypermarkets in East China. While it is still small, they are focusing on improving their selection of imported products in both Hangzhou and Shanghai. In Shanghai they are also starting to import directly.

Department Stores

Ito Yokado and **Isetan** are high-end, Japanese-owned stores that target upper class consumers. These retailers’ emphasis on expansion in to these second-tier markets suggests that there is easier access for high-end retailers in the second-tier markets. China wide, Ito Yokado has two stores in Beijing and one store in Chengdu. Isetan’s Chinese stores are in Shanghai and the second-tier cities of Jinan, Tianjin, Chengdu, and Shenyang. Depending on the market, higher end grocery stores in a department store may carry a large selection of imported products, or a section of a store that specializes in other types of merchandise may be dedicated to imported dry goods. There are many other examples of department stores containing a high end grocery store or supermarket.

Specialty Supermarkets and Boutique Stores

Jenny Lou’s is a major retailer of imported food products for expatriates, upper-middle income Chinese consumers and others who have lived or studies overseas. The company was established in

1995 and operates 12 supermarkets in Beijing located in high-income and/or upscale communities – often near diplomatic compounds and missions. More than 98 percent of the products offered in the small supermarkets are from overseas -- with more than half from the United States. In particular, breakfast cereal, seasonings, dairy products and wine make up the greatest focus of offerings. Jenny Lou reports that the economic downturn had some impact its business with sales down between 5-10 percent. The store has been affected by the departure of expatriate workers and customers trading down to less expensive products.

City Shop sells an extensive range of imported foods. Over 85% of City Shop's products are imported, and City Shop carries nearly 3,000 American food and non-food products. Started as a corner shop by a former Cochran fellow, City Shop now has 9 retail outlets in Shanghai and one in Beijing. It has developed its own system of retail and wholesale services. It maintains its own farms with internationally recognized organic farming and logistics systems. It produces 140 different organic vegetables and herbs, and produce is transported daily via temperature-controlled trucks to City Shop outlets and other wholesale business partners.

Ole, operated by CRV, targets upper-middle income shoppers and white-collar workers. Its 10 Beijing stores are all located in business or shopping centers. There are two stores in Shenzhen, with another set to open in Guangzhou. Another new store located in the China World Phase III in Beijing is scheduled to open at the end of 2009. Imported food product sales are approximately 50 percent or more of total food sales. The stores in Shenzhen have been successful in introducing imported foods such as cheeses, chocolates, coffee, wine, liquor, biscuits and fresh fruits at higher prices. Undermining this early success is an unstable supply chain and lack of promotion to support further demand growth. Ole is reportedly planning to open Shanghai stores in the near future.

Supermarkets

Lianhua, Hualian and Nonggongshang are three large state owned supermarket chains. These, and other domestic firms, dominate the supermarket sector. Although Lianhua and Hualian were nominally merged three years ago to form the behemoth Bailian, the largest retailer group in China, they continue to operate as distinct (and competitive) chains. Bailian appears to be more focused on rationalizing its diverse portfolio, and developing its shopping mall management component. Both Lianhua and Hualian have expanded aggressively through acquisitions of other chains, leaving both companies with the challenge of incorporating them into already weak state owned management structures. Inspired by foreign-invested companies, the Chinese chains are paying greater attention to branding, and most now carry a substantial number of house brands.

All three have also opened branded hypermarkets in and beyond Shanghai, and Lianhua is putting a particularly strong effort into its Century Lianhua hypermarkets. Although Nonggongshang's market share has slipped, it is attempting to expand its reach to match Lianhua and Hualian, opening NGS hypermarkets in distant cities like Nanchang, with mixed results.

The state owned supermarket chains also play another role – that of the local partner of international retailers. The international players had to agree to this to enter China. So Lianhua, for example, owns a large minority position in both Carrefour and Metro.

China Resources Vanguard also has a large number of supermarkets. It acquired with Suguo, a regional giant headquartered in Nanjing in 2004. The brands continue to operate independently.

Wu-Mart is a major retail chain based in Beijing that operates more than 2,000 stores throughout China featuring hypermarkets, supermarkets, and convenience stores targeting middle class and low end consumers. Retail sales reached \$4.4 billion in 2008 based on expansion and acquisition. In 2005, Wu-Mart acquired a 25 percent share of Beijing Mei Lian Mei to increase its market presence in Beijing. Wu-Mart also acquired a position in Xin Hua Bai Huo in Yin Chuan and Zhejiang Gong Xiao in 2008 to expand its number of outlets significantly throughout China.

Advantages and Challenges for U.S. Products

Overall, U.S. products enjoy a high image in the China market. Rising incomes and growing concerns over food safety among Chinese consumers after numerous episodes of food contamination mean there will be more opportunities for U.S. products, which are largely perceived as safe and wholesome. On the other hand, price is still one of the barriers for U.S. products to reach more Chinese consumers; other challenges include labeling regulations, distribution, and limited product knowledge. The following table provides further details.

Advantages and Challenges for U.S. Products	
Advantages	Challenges
U.S. products are regarded as high in quality, and manufactured with high safety standards.	Many U.S. products are costlier than their local counterparts.
Urban Chinese consumers spend 36% of their income on food.	Overall incomes remain relatively low, with imports selling mainly to higher income groups.
Consumers are interested in new tastes.	Consumers are very price sensitive, and often unwilling

	to risk spending money on unfamiliar products without trying them first.
Many U.S. brands are widely recognized and respected in China's major urban markets.	Many U.S. companies have established plants in China, manufacturing their products in China with Chinese ingredients.
Incomes are growing rapidly in second and third tier cities, creating a whole new range of opportunities.	Distribution and logistics remain underdeveloped outside of the largest urban centers, making distribution of imported products to interior cities difficult.
Western foods are more widely available than ever, and growing in popularity with consumers.	Lack of knowledge about U.S. products and how to prepare them properly makes consumers hesitant to buy.
China's entry into the WTO reduced tariffs on a wide range of imported products.	Labeling regulations and sanitary restrictions limit access to the market. Enforcement of regulations is haphazard, creating confusion for exporters.
The number of qualified distributors for imported food on the mainland is growing, along with the volume of direct exports.	Many U.S. exporters continue to rely on gray market channels, reducing their level of contact with end users and understanding of the market.
Rapid growth in retail chains has created the potential for bulk sales, with consequent improvement in pricing and handling.	Purchasing by most foreign-invested chains remains decentralized, preventing them from sourcing in bulk. Close relationships between store managers and local distributors help to reinforce this tendency.

Competition and Best Prospects

The most serious competition for U.S. food exporters comes from local and joint venture food producers and processors. The quality of fruit and vegetables in particular has increased rapidly, and many local traders now contend that the best of China's fruit is similar in quality to imports. The general lack of coherent marketing systems continues to plague China's industry, however, making it difficult to source significant quantities of products with consistent quality. While oranges similar in quality to U.S. navel oranges are available, the transaction costs of dealing with large numbers of small farmers, then sorting and packing raises the final market price to levels similar to imports. The formation of farmers' voluntary organizations such as the Zhejiang Pear Association has the potential to reduce these problems, but such organizations are still relatively new.

Competition is equally intense for processed foods, although differences in taste mean that the primary competition comes from third country competitors or joint venture manufacturers. Shelves may appear to be stocked with famous foreign brands such as Kraft, Lays and M&Ms, but close inspection reveals that most of these products are manufactured locally or in Southeast Asia. This allows manufacturers to cash in on brand identification, take advantage of low labor costs in China, and adapt their products to Chinese tastes and labeling regulations, all at the same time. Years of food adulteration scandals have made Chinese consumers cynical, however, and most will attribute a higher level of quality safeguards to food products that are genuinely imported.

The general trend to date has been for local manufacturers to push imports out of the price-driven mass market and into niche markets where quality and novelty are more important than price. This has already happened to varying degrees with pet food (Mars' locally manufactured Pedigree and Whiskas labels dominate the middle market), wine (Chinese labels dominate at the low end), apples (Washington State apples sell extremely well in gift markets) and confectionery (Mars). Growing local competition has emerged for table grapes, and domestic sweet cherries, lemons and almonds appear to be improving in both volume and quality, albeit from a very low base. Certain products, particularly western-style prepared foods, face little or no competition from local manufacturers, constituting a niche unto themselves. Improvements in quality and increased efforts at brand development are allowing Chinese companies to compete more effectively for some niche markets, but local manufacturers face the same distribution problems as imported products, as well as a high level of skepticism among consumers.

Third country competition comes in two distinct areas: commodity-type products such as frozen meat, poultry, seafood and fresh fruit, and western-style niche products such as canned and prepared foods and ethnic cuisines and ingredients. Competition in the fresh and frozen meat, fruit and vegetables arena, as well as dairy, comes primarily from Pacific rim neighbors, including Thailand, New Zealand, Australia, Canada and Chile, as well as South Africa and Brazil. Competition for western-style prepared foods is much more global, with competitors playing to their strengths in individual products such as olive oil, wine, pasta and pasta sauces.

The U.S. remains the largest single exporter of consumer-oriented food to China, and is the only exporter with a presence in most categories. China is attracting a growing level of interest from other countries, however, and has signed or is negotiating bilateral trade pacts with many of its neighbors. The following is a brief outline of key products and competitors.

Key Products and Competitors

Selected U.S. Imported Products	Main Foreign Competitors
Red Meat	Canada, Denmark, New Zealand, Australia
Poultry: chicken paws & wing tips	Brazil, Argentina
Oranges	New Zealand, South Africa
California Table Grapes	Chile

Washington Apples	Chile, New Zealand
Cherries	New Zealand
Breakfast Cereal	United Kingdom, Australia, EU
Cheese and Dairy	New Zealand, Australia, EU
Frozen Processed Products	Canada, New Zealand
Wine	Australia, France, Italy, Spain, Chile
Spaghetti sauce/tomato products	Italy, France, EU
Coffee	Japan, France, South Africa
Candy and Chocolate	Switzerland, Italy, France, Belgium, Japan
Nuts	Iran (pistachios), Mongolia, Korea (chestnuts) Russia
Seafood	Russia, North Korea, Canada, Norway, Japan
Ginseng	Canada, Korea
Dried fruit: prunes and raisins	France and Italy (prunes)
Baby food/infant formula	New Zealand, Switzerland
Premium Ice Cream	France, New Zealand

Best Prospects

Products Present in the Market Which Have Good Sales Potential

- Nuts and dried fruit (prunes, raisins)
- Seafood
- Poultry meat
- Red meat (U.S. beef and related products are currently not permitted entry into China)
- Frozen vegetables (esp. sweet corn)
- Infant formula
- Baby food
- Dairy products (cheese and butter)
- Baking ingredients and bread bases

- Frozen potato products
- Fresh fruit (oranges, apples)
- Premium ice cream

Products Not Present in Significant Quantities, Which Have Good Sales Potential

- Fresh fruit (cherries, pears)
- Processed/dried fruit (blueberries, cranberries)
- Mexican, Indian food
- Ready-to-cook and ready-to-eat foods
- Organic foods (niche market)
- Functional foods

Guidelines for Entering the Market

China is not a single amorphous market, but a jigsaw puzzle of small, overlapping markets separated by geography, culture, cuisine, demographics and dialects. As such, there is no single formula for success in China. The best approach to marketing a product will vary depending on the product and the specific market (geographic and demographic) being targeted. Nonetheless, there are some basic guidelines that can be applied to most cases.

1) Understand the importance of relationships. China's legal system is developing, but remains inconsistent. Enforceability of contracts varies widely, but is generally weak. Business in China instead relies heavily on personal contacts and influence (referred to as 'guanxi'). For companies with a serious interest in China, no investment will be more important to their success than the network of relationships that they establish in China. For more pointers on the role of guanxi in Chinese business culture, please see report [CH4835](#), Chinese Business Etiquette.

2) Find a local partner and/or distributor. For smaller companies without the resources to directly market their products in China, a good distributor is critical to success. Distributors provide the network of relationships with buyers, regulators and others, that is essential to doing business in China. Unfortunately, these tend to be in short supply. ATOs keep lists of well-known distributors. Keep in mind that contract arrangements with retailers tend to place most of the market risk for new products onto the distributor, so they may require some convincing before they

will take on an unfamiliar product. Specialized distributors also exist for certain product categories, most notably wine, seafood and fruit. Be careful in selecting a partner and in establishing an incentive structure: partnerships gone sour are the most common cause of business failure in China. Paying close attention to payment terms can be an important aspect of this (confirmed letters of credit are standard).

3) Know the rules. Chinese regulations are often vaguely worded, arbitrarily enforced and opaque. Your distributor can (and should) handle this for you. However, weak enforcement has made short-cutting a common practice, and exporters that rely entirely on Chinese partners for this are often unaware that their products do not conform to the rules until a problem arises. To defend against the unexpected, exporters should try to be reasonably familiar the actual regulations. Product registration, labeling and product expiry dates are the top concerns in this area. To enter the retail market, food products must receive a hygiene certificate from the local government where the product will be sold. Food products must also be labeled in accordance to Chinese government standards, with the labels pre-approved by the government. Functional or health foods must obtain a health-food certificate, and claims of health benefits on packaging or in advertising are strictly regulated. Foods containing GMO ingredients may be subject to additional labeling requirements, as are organics. There are also a wide range of concerns related to China's new Food Safety Law. Please see the FAS FAIRS reports for China on the FAS website for details (www.FAS.USDA.gov; attache reports) or the website for China's Administration for Quality Standards, Inspection and Quarantine (AQSIQ) at www.AQSIQ.gov.cn.

4) Get to know the market. As noted above, China is a surprisingly diverse place. Tastes, customs, culture, business practices and government regulations vary from place to place. Experience in other markets will not necessarily help in China, and some aspects of the market need to be witnessed to be fully understood. The best strategy is to target a specific place and get to know it well. The scope of your effort will determine whether you select a single city or a whole region. Travel to China is highly recommended to evaluate partnerships, build guanxi (see above), and identify new opportunities and potential obstacles. (Partners are frequently hesitant to mention problems in formal communications, but will be more forthcoming over informal events like dinners). FAS market briefs offer a good source of information on the market, and are available for free on the FAS website noted above.

5) Find your market niche and focus on it. China is a very, very big place. The mass market may be huge, but it is driven entirely by price and dominated by lowest-cost local producers. Better returns are to be had from targeting a specific niche. The country has a nearly infinite number of

niche markets, some of them quite large. Examples include the high-end gift market, where margins are high but packaging is crucial (wine, ginseng); the expatriate market (famous brands from home like Kraft, Betty Crocker and Post); or health-conscious young parents (prunes, almonds, fresh fruit).

6) Invest (wisely) in consumer research. To outsiders, Chinese tastes can seem fickle. Tastes poorly received in the U.S. may prove successful in China, while products targeted to one market niche may end up finding their greatest success in a completely different one. To avoid unpleasant surprises and find new opportunities, exporters with a long-term interest in China are advised to research the market and test new products directly. Be careful how you invest research money, however. The quality of research by international market research firms is often not much better than that of much less expensive local companies. ATO-sponsored activities offer good opportunities to field test new products or packaging.

7) Adapt your products. Exporters should be prepared to adapt their products to the demands of their Chinese consumers. This includes flavors, packaging, prices and labeling. Small changes to flavors or packaging, based on market research, may make the product more viable in China. For example, Chinese consumers are often unwilling to buy unfamiliar products if they can't actually see them, so including a transparent window in the box or offering free samples can help sales. Products that are marketed as gifts, such as wine, should place extra emphasis on the packaging, as this is considered an important part of any gift. Many exporters seeking to break into the gift market have special packages manufactured in China, which can also help to address labeling issues.

8) Be flexible. Things don't always work as expected in China. This can be a good thing, provided you can take advantage of opportunities when they arise. Exporters who enter the market with preconceived notions of how to market their products often miss out. ATO activities routinely turn up unexpected opportunities: for premium boneless pork in Chengdu; for d'anjou pears and cherries in Shanghai; for Mexican food in Wuhan. By the same token, a product may find its best niche in an unexpected place. Washington State apples have done quite well in China despite tough competition from local products, because superior appearance and consistent quality made them the top choice for gift baskets.

9) Pursue gradual but sustainable growth. A common pitfall is the temptation to pursue explosive growth, focusing on geographic penetration rather than sustainability. This may produce impressive short-term results, but exporters with limited means may find themselves overextended very quickly. If the exporter is unable to meet the expectations of their customers, they may turn to

other sources (such as local copycats or counterfeiters) or demand may collapse. Alternatively, the exporter may find themselves overly reliant on local agents that they do not know well, and who have little interest in the long-term success of the product. The go-slow approach gives exporters time to learn the markets, accumulate customer feedback, and build their distribution channels.

10) Invest in market promotion. Once in the market, an exporter's product will be competing with tens, if not hundreds, of similar products. Domestically made products will often have advantages on price, familiarity and local brand recognition, while imports can be aided by aggressive promotional campaigns. Lacking the massive marketing budgets of multinationals like Nestle or Kraft, most exporters must design and implement their marketing campaigns carefully. Attending only quality, focused trade shows for your particular market segment is a good way to start. In-store promotions are also a cost-effective way to support your product and build relationships with distributors and retailers. Above-the-line media advertising should be carefully planned, as TV and radio time is expensive and has limited reach. Exporters are strongly advised to explore joint marketing opportunities with ATOs or with a State and Regional Trade Groups (such as MIATCO, WUSATA, Food Export USA/NE, or SUSTA). These events tend to be cost effective and draw more attention than stand-alone promotions.

Regional Profiles

China is a diverse place, and fragmented distribution and logistics systems help to reinforce existing divisions. To assist exporters in dealing with these regional differences, FAS maintains six offices in China, with Agricultural Trade Offices (ATO) in Beijing, Shanghai, Guangzhou, Chengdu and Shenyang, and an Agricultural Affairs Office in Beijing. Individual market profiles for each region are offered in the following sections, written by the respective ATO offices.



Eastern China - Shanghai and Yangtze River Delta

The city of Shanghai is a massive market unto itself, with a population estimated at 20 million, and incomes among the highest anywhere in China. As costs in the city have risen, the economy has begun to shift away from manufacturing and into financial and management services.

Manufacturers seeking to escape high costs in the city while taking advantage of the infrastructure and massive consumer base have created an economic boom in the surrounding region. The city is located at the center of a web of economic development that includes the provinces of Zhejiang and Jiangsu, and is collectively referred to as the Yangtze River Delta (YRD). This region accounts for nearly 1/3 of mainland China's GDP. Massive infrastructure investment has led to major improvements in logistics and drawn the region closer together. The opening of the Yangshan deepwater port facility is expected to make Shanghai the world's largest container port within the next few years. Shanghai's large expatriate community (estimated at 500,000) is dominated by Taiwanese, who bring with them a familiarity with foreign brands and a taste for U.S. and Japanese foods.

Shanghai's retail sector is increasingly saturated, and home to a large number of supermarkets, hypermarkets and an extremely strong convenience store sector. Supermarkets remain the dominant, and oldest, modern retail format, with relatively weak management and infrastructure.

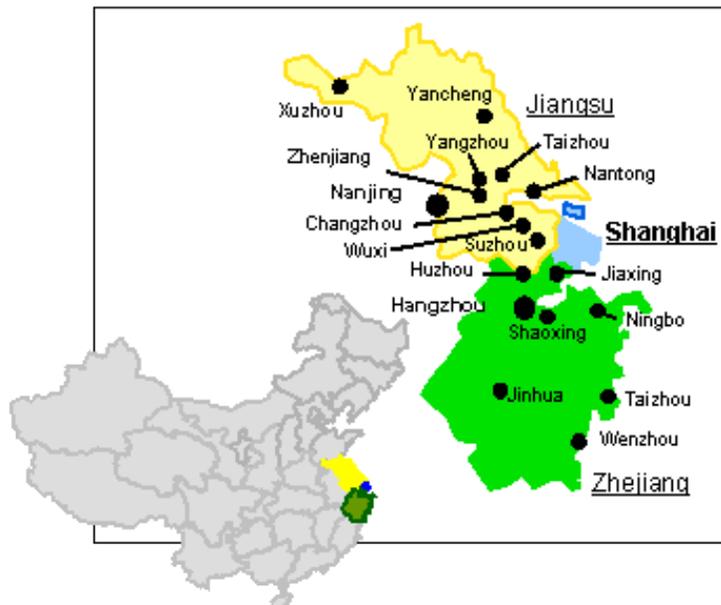
Supermarkets are losing ground to hypermarkets and convenience stores. This loss in market share, however, is counted in growth not captured; new stores continue to open. The supermarket format is quite durable owing in part to Shanghai's high population density (the highest in China and one of the highest in all of Asia), which makes it possible to have a small supermarket within walking distance of virtually any place in the city.

Influenced by the global financial crisis, economic development in Shanghai slowed down in 2008, but GDP still grew by over 9% in real terms. Stimulating domestic demand is one of the Chinese government's measures to combat the economic downturn. Overall, retailing in Shanghai still remains robust and retailers are working on new concepts to lure consumers, such as market segmentation, so as to produce points of differentiation and create an edge over competition.

Beyond Shanghai

The immediate area surrounding Shanghai (the Yangtze River Delta, or YRD) is a beehive of industrial and commercial activity. In the key cities, retail development is already well advanced. Suzhou and Hangzhou are home to Carrefour and other hypermarkets, as well as convenience stores. Hypermarkets throughout the region source imports through Shanghai, taking advantage of the region's outstanding logistics and Shanghai's large

The Yangtze River Delta



community of experienced food importers. The supermarket sector in these cities is typically dominated by either Lianhua, Hualian or Nongongshang, but with a preponderance of independents (with the notable exception of Nanjing's Suguo).

The capital of Zhejiang Province, **Hangzhou** is home to Carrefour, Metro, Lotus, Auchan, Wal-Mart, Lianhua, and Hymall, among other super- and hypermarkets. Hangzhou's retail market is doing far better than expectations: in an ATO-organized nationwide retail promotion involving 24 Carrefour stores, the Hangzhou store ranked 7th in sales: ahead of Guangzhou and following stores only in Shanghai (4 stores) and Beijing (2 stores). In addition, the Hangzhou store was extremely aggressive in recruiting distributors and products for the event, and ultimately carried far more items than originally agreed. (Please see [CH7819](#)). In a departure for a state owned chain, Lianhua is actively promoting imported products in Hangzhou and plans to open a specialty supermarket concentrating on imported products.

Suzhou's market is steadily growing, and a privately-owned cold chain already exists, with temperature-controlled warehouses and delivery trucks. Metro has established itself in Suzhou as the destination for one-stop shopping, and its membership is already 130,000 strong. To further stimulate market growth, the city's infrastructure is developing at light speed. Several new highways were built recently; bridges cross the Yangtze River, and a light rail system has been scheduled for completion in 2008. (Please see [CH7816](#)).

Development is now moving on to a third tier of cities. Particularly notable are **Wuxi**, which has become a major distribution center for seafood and meat products in the YRD area (see the recent report [CH8806](#) for more information); **Ningbo**, which has average incomes on par with Shanghai but a less well-developed retail sector; and **Nanjing**, the capital of Jiangsu province.

Nanjing's market and imported product consumption have increased substantially. In ATO/Shanghai interviews, major retailers including Metro, Walmart and Carrefour stated that the higher the percentage of imported food items in their store, the better their sales - indicating the high potential for imported food in Nanjing. Nanjing is also home to Suguo, a retail giant that holds more than fifty percent of the city's market.

Although **Wenzhou** is one of the richest cities in China, its market for foreign imports is still relatively underdeveloped. Wenzhou was only opened to international retail giants in 2006. While the market was slow to open, the retail sector is growing quickly. According to the Wenzhou Retail Association, a "Sourcing Alliance" consisting of all the important retailers in Wenzhou was organized in 2008 to consolidate the sourcing of imported food products, to strengthen the bargaining power of Wenzhou retailers against food importers. (Please see [CH7814](#)).

Wuhan, in Hubei province offers a mid-range prospect. It has a reasonably well-developed retail sector, with Metro, Carrefour and Wal-Mart all represented. As income levels rise throughout

urban areas in China, potential markets are emerging in growing cities everywhere. In 2007, 08, and 09 ATO Shanghai has conducted multilevel campaigns to promote U.S. food products in Wuhan. All these events have exceeded our expectations, and we have succeeded in introducing several hundred SKUs to consumers in Wuhan. The city seems receptive to American products, and with the rapid increase of supermarkets, hypermarkets and convenience stores, as well as more than 40,000 restaurants, it has a reasonably developed retail sector. (Please see [CH7815](#), and [CH9801](#).)

Wal-Mart's remarkable success in **Nanchang**, the capital of Jiangxi province, provides a good case study for retail in China. Nanchang was not generally regarded as a retail market in the same class as Kunming or Chengdu. However, close cooperation with local officials netted Wal-Mart a prime location, just as the city launched a major redevelopment effort, making for a major success. The success of this venture is all the more striking given the relatively weak performance of Nonggongshang's NGS hypermarket, established several years earlier in the same city, and demonstrates the value of local market knowledge.

Beijing and Northern China

Although expansion is slower compared with recent years, the northern China retail market continues to grow despite the current global economic slowdown. The sector slowed most sharply from the Fourth Quarter 2008 to the First Quarter 2009. However, since the Second Quarter 2009, retail sales have strengthened. The economic had its greatest effect in Beijing and to a lesser extent to coastal cities, while the inland regions of northern China reported little impact.

The economy did shift demand – with high-priced food products more affected by poor as consumers shifted to lower-mid priced substitutes. For example, in Beijing wine priced under RMB 100 (\$14.62) remained very popular while products above RMB 100 (\$14.62) faced diminished sales. In Tianjin, a reduction in group purchases hit imported fruit sales during the last Chinese Spring Festival. The slowdown on the coast has also reduced eating out, shifting consumption to the home. For example, fresh food products sales in North China have shown positive growth because fewer consumers dine out.

The government stimulus plan, falling rents and lower wage pressure have encouraged both multinational and local retailers to expand operations in northern China – with some even accelerating plans to open stores in 2009. At the same time, intense competition and escalating costs in Beijing have also fueled growth outside the capital. Retailers are increasingly focusing on second-tier emerging cities, particularly richer coastal locations such as Qingdao, Weihai, and

Yantai. ATO Beijing expects these trends to continue or even accelerate in the years ahead.

Beijing consumers continue to shift their shopping from “wet” or open air markets to supermarkets and convenience stores with retail consumer sales totaling \$65.7 billion or 20 percent over 2007. Competition is extremely intense in Beijing because local consumers demand diverse and high quality food at competitive prices. As a result of rising costs and standards, some retailers have gone out of business. For example, last December one supermarket located in one of Beijing’s most upscale shopping malls “The Place” literally disappeared overnight.

International hypermarket operators active in Beijing include Carrefour, Wul-Mart, Tesco and Metro. Wal-Mart has followed a strategy of staying out of downtown to avoid direct competition and instead opened new outlets in suburban Beijing in 2008. In order to lure customers, most hypermarkets provide free parking and shuttle bus services adjacent to shopping and entertainment complexes. Special aisles dedicated to imported food products are often arranged by country of origin. A large variety of imported foods such as cheese, butter, and other dairy products, cereal, cookies, coffee, candy, beverages, wine and snack food are represented in such supermarkets. Products come from a diversity of origins with the United States, Spain, Germany, Switzerland, France, Canada, Italy, Australia, and Korea the most dominant. Carrefour and Wal-Mart have lowered prices on selected products by as much as 20-30 percent in Beijing during the New Year and Spring Festival holidays to encourage sales that often continue even after the holidays have ended. Price cutting will likely return as the holidays come again.

Customers in **Qingdao** have shifted from wet markets to supermarkets because of a booming economy and high per capita GDP. Although the retail market stumbled between the Fourth Quarter of 2008 and First Quarter of 2009, it has recovered from the Second Quarter of 2009 onward. The short downturn came because of low consumer confidence. The downtown location of Jusco and Carrefour in Qingdao keeps these outlets busy even during office hours. The leading second-tier city in northern China the market attracted major multinational and domestic retailers. Hypermarkets are popular with the Carrefour only ten minutes away on foot from Jusco resulting in significant competition between these two retail giants. Hisense Plaza opened just before the 2008 Olympic Games and featured a variety of luxury brand goods such as Cartier, Gucci and Louis Vinton targeted at high-end customers in Qingdao and Shandong Province. Hisense Supermarket cooperated with ATO Beijing in holding a U.S. Food Promotion in July 2009 showcasing over 600SKUs of new seafood, dairy, snack foods, fruit and pet food products. Partially because of the event, Hisense Plaza is now known as a top destination to source high quality American Food Products in Qingdao. Marine City, a new giant shopping mall facing the sea, is five minutes on

foot from the Hisense Plaza will open in November 2009, including a supermarket with more than 6,000 sqm targeted at upper middle class customers.

Tianjin's median income is much lower than Beijing and Shanghai with consumers very sensitive about price. Carrefour has focused on attracting shoppers by offering lower prices compared with wet markets. Imported products are limited to the downtown area in stores such as Carrefour, Lotus and CRC. Imported products generally do better in the Binhai New Area because of the large number of white-collar workers employed by multinational companies and the large number of expatriates living there. In addition, E-Mart of Korea entered into a joint venture with Tianjin TEDA and has five supermarkets targeting upper middle class customers and Korean expats. Tianjin is an export port, it was hit harder than most by the financial crisis in 2009. Official sales figures do not show this because major retailers persuaded suppliers to take back their products.

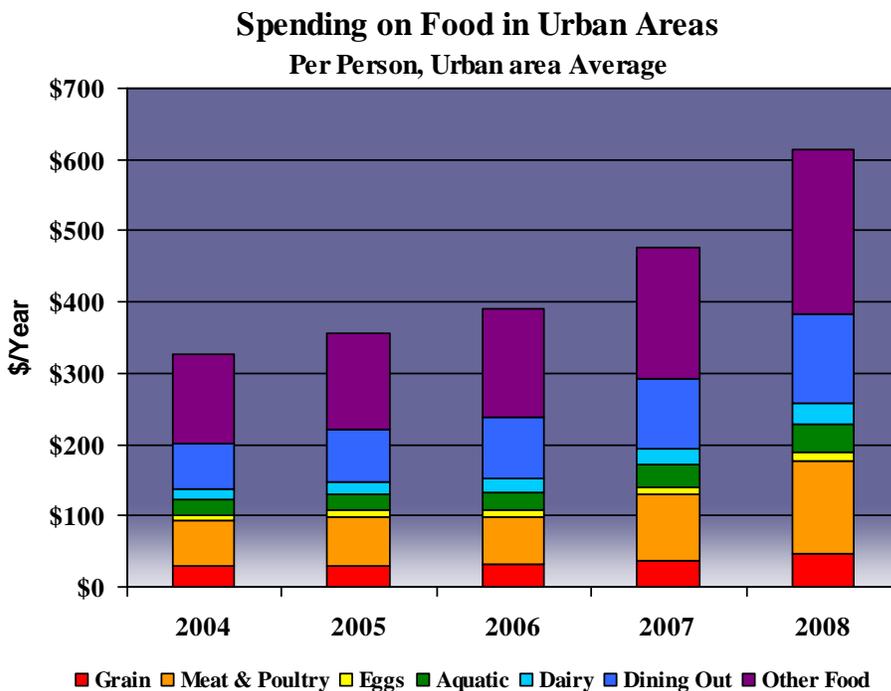
Zhengzhou - Based on geographical location and its advantage as a major rail hub and large population, the retail base developed rapidly in this major inland urban center. Young consumers in the city are curious to try new products especially imported food products -- even if their incomes are lower than peers in Beijing and Qingdao. At this point, this curiosity has not yet resulted in a long-term market for imported food products although this seems to be poised to change very soon. Packaged food, fresh fruit, beverages, beer and wine are the main imported food products with imported dairy, meat and seafood rare in the market. Organic products are scarce in the market given high prices and a lack of awareness. Group purchasing is the primary channel to sell imported food products. In addition, Zhengzhou is also a distribution center for imported foods to inland second and third tier cities in surrounding provinces given its convenient transportation links.

Xi'an, the capital of Shaanxi province is considered the gateway to northwestern China. Over the last 4-5 years, the retail sector has developed rapidly -- from 2004 to 2009, the total number of hypermarket grew from 25 to 63. China Resources Vanguard (CRV) is dominates the hyper market sector in Xi'an with 22 stores. The highest end store is Century Jinhua, which runs five department stores in Xi'an and offers the most diversified imported products in Xi'an.

The coastal resort of **Weihai** with its booming economy attracted the attention of retail investment and has become the next battleground for Chinese retailers. Korean food products are very popular because of the more than 40,000 Korean Expats which has changed the way people shop and eat. The local government has also encouraged foreign investment -- with Jusco, Lotte and Mix City hypermarkets entering the market within 2 km of downtown. Carrefour and Wal-Mart are also looking for new locations downtown as well.

Consumer Spending Patterns

As Chinese get richer they tend to spend much more money eating out and to diversify their diets. Consumption of meats has been increasing more rapidly than overall food expenditures, and consumption of western style products is also growing rapidly. Strong and continuous economic growth caused urban Chinese to increase their spending on food by almost 17% per year on average between 2004 and 2008 when measured in U.S. dollars. Expenditures on food almost doubled over that time period. While the growth rate has almost certainly been a little lower in 2009, it is probably still impressive.



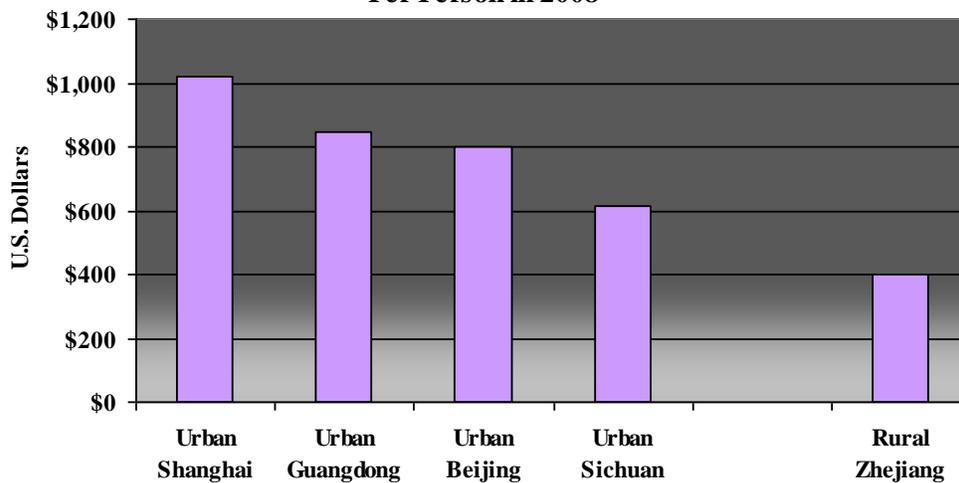
Source: China Statistical Yearbook 2009

While average annual food purchases for all cities was slightly more than \$600 per year, per person food consumption in Shanghai was slightly more than \$1,000 per person, and that in Beijing and Guangdong was about \$800 per person. This compares with U.S. food purchases per person of about \$2,300/year. Urban food purchases per person in Sichuan, a province in Western China that contains the city of Chengdu, come in at the national average for urban areas - demonstrating the potential of markets in western China. While there are some smaller cities where per capita income is about equal to that of Shanghai (such as Ningbo), the population and wealth of the three largest urban areas - Shanghai, Guangdong, and Beijing - lead most exporters to concentrate on at least one of those

markets.

Even some of the wealthiest rural areas in China - those in the commercial province of Zhejiang south of Shanghai - have a lower level of consumption than urban areas in poor provinces. Disposable income in these areas is rising rapidly however. If the current consumption data is correct, the rural population in Zhejiang province may achieve Shanghai's current level of consumption in 15 years. The population in most urban areas will likely still be more wealthy.

**Annual Purchases of Food in Selected Areas
Per Person in 2008**



Source: China Statistical Yearbook, 2009

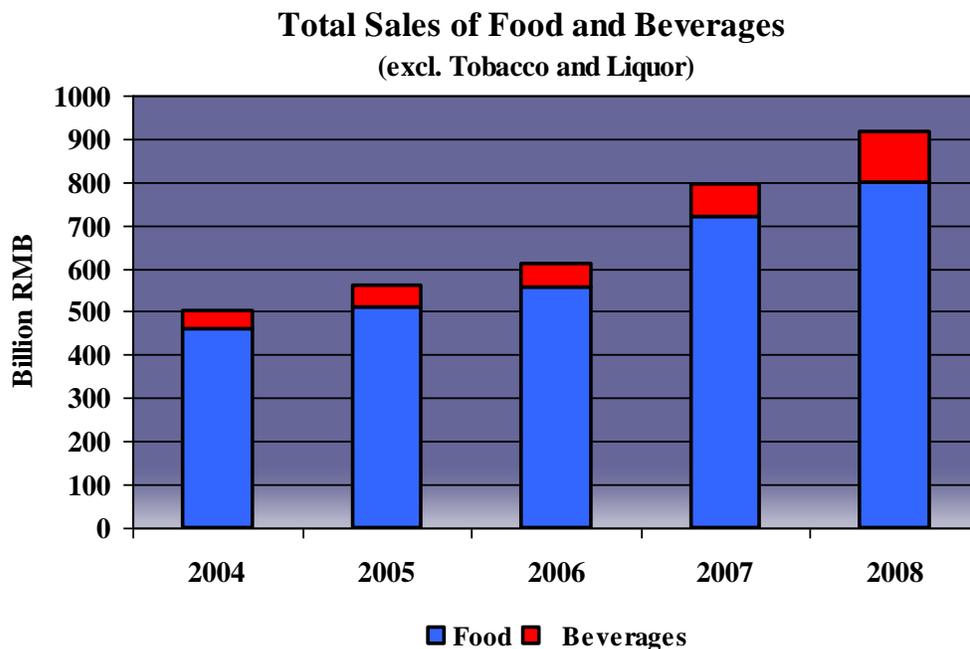
China is a very large country and different parts of China are at different levels of development. However, there are large variations of income and pockets of wealth in all large urban areas, and Chinese cities are no exception. The variation of wealth in China is illustrated in Table 1 in the Appendix. The wealthiest areas in China are Beijing and Tianjin in the north, Guangdong and Fujian in the south, and the Shanghai, Jiangsu, Zhejiang area in eastern China.

There are many urban centers in China that westerners have not heard of. Even a "small" city by Chinese standards may have millions of people. These are becoming much more prosperous, and their growth rates are starting to exceed those of the three large urban areas. It would be a mistake to overlook these markets and the potential to develop strong market positions in them. While there are certainly opportunities in these secondary

markets, the number of distributors handling your type of product may be very limited. Given differences in regional tastes, logistical difficulties, and the size of China, many exporters choose to focus in a particular region of China first rather than try to develop the entire market at once.

Market Size and Segments

Determining the size and rate of growth of Chinese purchases of food and beverages is complicated. The official data does not attempt to pick up the smallest enterprises, and the usual concerns about data quality in a developing country are compounded by China's legacy of central planning. The Yuan also rose by about 9.5% against the U.S. dollar from 2007 to 2008. This gives an added boost to Chinese expenditures when measured in dollar terms. According to China's 2009 Statistical Yearbook, the total sales value of food and beverages rose by 15.3% in 2008, from 793 billion RMB in 2007 to 914 billion RMB in 2008. If you are U.S. exporter, however, the change in U.S. dollars may be more useful to look at. Using average annual exchange rates, we find that the total sales volume in U.S. dollars rose by 26.2% in 2008, from \$104 billion in 2007 to \$132 billion in 2008.



Source: China Statistical Yearbook 2009

Market Segments

While 2008 sales data for the major retailers is available, it is of limited use when discussing market segments. This is because retailers in China often cross several market segments. Some domestic players have hypermarkets, supermarkets, convenience stores, and specialty stores. However, we can say that most imported products have found their greatest success in the hypermarkets and in specialty supermarkets. Some products, such as fruits and snacks, have much deeper penetration, and some supermarkets and convenience stores may be becoming more interested in imported products.

Hypermarkets: The hypermarket format is much more concentrated than other grocery channels. While some domestic retailers (including CRV and Lianhua) have a significant presence, this format is dominated by foreign operators including Carrefour, Wal-Mart, Metro, Auchan and Tesco. In Shanghai for example, the 82 foreign hypermarkets accounted for 78.6% of the total hypermarket sales volume in 2008. Other retail channels, most notably supermarkets, are highly fragmented and controlled by domestic players.

Multinational chains such as Carrefour and Wal-Mart benefit from their reputation for offering better quality products than most domestic retailers, thanks to stricter quality control in a country where food safety is a major concern after several disturbing food scandals in recent years. In food products, especially fresh food, hypermarket retailers benefit from better hygiene controls and a higher volume flow rate, and are thus able to ensure better food safety for consumers. As such, an increasing number of Chinese consumers visit hypermarkets instead of independent food stores for grocery shopping. Fresh produce has become an attractive section to draw in Chinese consumers.

International retailers generally have a higher level of familiarity with imported brands and products, and recognize the value of bringing new products to market and promoting them. Hypermarkets are also the major sales venue for imported food products, due to international retailer's familiarity with imported products and better management and organizing skills. Most are experienced in promoting new products, and flagship stores like Carrefour's Gubei store or Lotus' Superbrand Mall store in the Pudong area have it down to a science. Despite this, imports rarely constitute more than 5% of total SKUs even in high profile stores. Nevertheless hypermarkets are the single best retail venue for imported products.

Most hypermarket chains vary the proportion of imported goods they carry in individual

stores depending on the income level and foreign population that the store serves. For the time being, hypermarkets are still mostly limited in first and second-tier cities because of lower rural incomes. Until wealth spreads more deeply into rural areas and infrastructure improves, most places outside the first and second tier will not have access to modern retail formats.

The hypermarket has been well accepted by affluent customers due to large parking facilities, monopoly stores and numerous restaurants and coffee shops that enable consumers to combine shopping and leisure activities. Most hypermarkets in China offer free shuttle bus service to nearby communities and constantly offer promotional items to attract consumers. These measures successfully draw heavy traffic to the store, but some consumers go to the store to buy the promotional items only, reducing the purchase per customer. This active promoting may also drive away some high-end consumers who desire a less crowded environment and more concentrated product display. As a result, specialty supermarket stores such as City Shop in Shanghai and Wuhan Life & Theatre supermarkets, both targeting high and upper-middle class clients, have successfully attracted customers from the hypermarkets.

The most decisive component in hypermarket food promotion for imported goods is free sampling. Consumers are cautious rather than impulsive buyers, and will rarely spend money on a product they have not had a chance to try. Hypermarket promotions also come with many strings attached. Some charge listing fees, most demand that promoters be provided at the distributor's expense (some even charge fees to have the promoters on their premises). Some require two months' credit, while others pay up front. Other conditions include accepting returns of unsold products at the end of the promotion. Although these problems are usually handled by the distributor, they will affect your sales.

In addition to the major chains, hypermarkets often face competition (especially in Northeast and Central China) from local department store operators with one or two locations and specialty supermarket stores. Department stores have evolved in the direction of hypermarkets, adding large food stores, while many hypermarkets have taken on some attributes of department stores.

Hypermarkets in China tend to be somewhat smaller than their western counterparts, and very few (excepting Metro) follow the big-box format faithfully. In large cities, they are

typically multi-story operations. Most act as small shopping malls, setting aside a large amount of space for independent boutiques and eateries, a habit that tends to reinforce the perception of hypermarkets as places for occasional shopping expeditions rather than daily shopping. For the hypermarket itself, the food sales area typically accounts for about half of the total area.

Management within the stores tends to be quite good, but distribution has not kept pace. Hypermarkets in China tend to develop groups of favored distributors. They dislike working with unfamiliar companies unless they can offer a large number of SKUs, strong marketing support or some other incentive. Distributors tend to be very conservative in introducing new products, due to the high level of market risk. As a result, exporters with a limited product range need to work both ends of the problem at the same time: identifying a retailer that is interested in the product, and identifying a distributor that either has an existing relationship or is willing to work with the retailer.

Supermarkets: Imported food is relatively rare in Chinese supermarkets. Products that do well in this sector tend to be commodity products already widely available, such as fresh fruit, frozen vegetables and nuts. Supermarkets rarely if ever import directly, or even buy directly from an importer, tending instead to rely on wholesale markets and local manufacturers or distributors. Stores with a significant expatriate community nearby are likely to carry imported breakfast cereals and a perfunctory selection of imported sauces (especially pasta sauce) and seasonings. The best possibilities are in the smaller, privately held chains, which are more likely to see the value of high-margin imports and tend to have better integrated distribution systems. Such chains may carry products as varied as wine, exotic fruit (avocados, in one case) or confectionery, but only in low volumes. Even so, price will remain a consideration. State-owned supermarket chains generally have less integrated management and distribution. Opportunities exist, but only on a limited basis with a small number of stores, and only for products already present in the market. For either state-owned or private supermarkets, direct contact with company managers is the best means of introducing a new product.

Import penetration is lower in supermarkets than other modern retail venues. U.S. food products in these venues are typically limited to frozen corn and mixed vegetables, frozen potato products, some packaged goods and occasionally fruit (apples or oranges). Other items tend to appear on a haphazard basis: past checks have turned up breakfast cereals, low-end wines and Washington state apples. The sparse selection of imports is rooted in

the customer base of these stores, which focus on working class shoppers, who are notoriously price sensitive and less inclined to try new products than the more well-heeled customers that frequent hypermarkets and upscale convenience stores. Distribution is also a problem, as stores tend to source from local distributors, directly from manufacturers, or from local wholesale markets. Supermarkets are often franchised in China and can have much smaller footprints than is common in the United States.

In order to compete with hypermarkets, Shanghai's supermarkets are putting more efforts into enlarging their fresh section, catering to the tastes and demands of local consumers. The local government is also encouraging supermarket chains to create 'fresh' supermarkets, expanding the floor space dedicated to fresh products from less than 1/3 to over 1/2. Over 300 stores in Shanghai have finished the change. And sales of fresh produce are gradually increasing. Supermarkets throughout the region (including Suguo, a unit of CRV) appear to be moving in this direction, but are being slowed by problems in sourcing large quantities of quality product.

Specialty Supermarket Stores and Boutique stores: These stores have multiplied in the last few years. They are often located adjacent to high-end department stores or upscale business centers. Built to attract upscale consumers in first and second-tier cities, they have a high proportion of imported food products – ranging from 10 to 80 percent of products. They are not only present in first tier cities such as Shanghai but also in some second tier cities like Wuhan.

Some high-end and specialty products first enter the Chinese market through these types of outlets before moving on to larger venues. Some of these companies also include import/distribution operations, and can assist exporters with issues such as labeling and product registration. Otherwise, exporters will need to identify a good distributor. In the case of high-end and specialty products, HRI-focused distributors (who are familiar with the products but may lack experience with labeling issues) may be as helpful as larger retail-oriented distributors (who often lack experience marketing high-end products), particularly in emerging city markets. Because of the small scale and highly varied nature of this market segment, interested exporters should contact the relevant ATO for a list of potential venues.

In Shanghai, City Shop Supermarket continues to be one of the best single venues for imported food, and now does significant business as a distributor of imports to other

stores. Hong Kong based City-Super and CRV's Ole may be planning to enter the Shanghai market in the near future.

The leading boutique retailers in northern China are BHG (Beijing Hualian Supermarket) and Ole in Beijing, Hisnese Plaza in Qingdao and Jin Bou Da in Zhengzhou. Specialized imported food supermarkets also target high-end customers and expatriates in Beijing, Qingdao and Zhengzhou. BHG is also opening stores in Nanjing.

Convenience Stores: Management in convenience store chains is probably the best of any retail sector. All stores have refrigerator and freezer sections, microwave ovens, and most have a selection of hot snacks (mostly meatball or tofu on skewers). Store layouts are highly standardized, although some chains have developed more complex systems that customize product selection to the peculiar location based on past sales patterns.

The concept of trading higher prices for convenience will take time to be accepted by more consumers. Competition also tends to make convenience stores conservative about pricing, though ATO Shanghai's experience indicates that chain managers are more price sensitive than their customers.

The convenience store sector is expected to expand dramatically as consumers look to reduce time in meal preparation. Stores compete aggressively for good locations, and it is not uncommon to see three different convenience stores within 100 feet of each other in prime areas.

Import penetration in this sector tends to be relatively low, despite a high level of interest on the part of several chains. Being largely domestic companies, management at convenience store chains tends to be less familiar with imported products than their counterparts in the hypermarket sector. A second difficulty faced by imports is packaging: convenience stores typically require smaller package sizes, being focused mainly on single-serving products. Exporters are advised to open discussions directly with chain officials to identify products with potential, and ensure that packaging meets their needs.

Then the exporter will need to identify a local distributor that can handle the import paperwork and labeling issues. One alternative to this is to work with an importer/repacker, who can import in bulk, then package the products in China with

Chinese labels and packaging appropriate to the convenience market. This strategy has proven extremely successful for U.S. prunes.

Managing logistics for convenience stores is very challenging. Limited shelf and storage spaces make convenience stores heavily reliant on sophisticated logistic systems that should provide delivery 2 or 3 times a day. But in Shanghai most convenience stores are guaranteed just one delivery per day. This adversely affects the ability of these stores to offer the fresh and ready-to-eat products that are among their most attractive offerings. In addition, the need for small package sizes limits their set of suppliers.

Some hypermarket operators in first and second-tier cities are expanding their small-format convenience stores to increase market share and better utilize existing supply channels. Most are located near upscale communities and business centers and target white-collar workers, upper-middle class and young consumers in search of convenience. The stores feature daily necessities and ready-to-eat items.

The world's largest convenience store chain, 7-Eleven, which opened its first store in Beijing in 2004, now has 70 outlets. The company sees profits increasing during the economic downturn given a growing number of consumers buying food at stores instead of eating out.

Ferocious competition has spurred efforts to innovate and to target niche markets. Quik and Kedi, the two leading convenience stores in Shanghai, have both entered into deals with gas station operators to open markets in their stations. Lawson's pioneered efforts to target white collar employees and service staff in shopping districts with high-quality Japanese style lunch boxes. Kedi also offers lunch boxes, which are quite popular among office workers in the central business areas. Family Mart expects to benefit from superior management and technology (they may be surprised by the local competition). Nearly all convenience stores offer a range of services to draw foot traffic, with Alldays ushering the latest innovation by providing China Life travel insurance policies at their stores.

Shanghai's convenience store industry is by far the most developed in the country, with the city playing home to an estimated 5,650 convenience stores—nearly 1/3 of the national total. One source estimates the number at 1 store per 4,400 residents (not including immigrant workers), comparable to saturation levels in Japan and the U.S. Despite this, the sector continues to grow.

Shanghai's convenience sector is overwhelmingly dominated by subsidiaries of the giant

state owned supermarket chains: Quick (Lianhua), Alldays (Nonggongshang), Kedi (Nonggongshang via its Bright Dairy subsidiary), with only a few foreign players such as 7-Eleven and Lawsons (Lawsons was a JV between Hualian and Lawsons Japan, but Lawson Japan may have sold its shares back to Hualian). Japan's Family Mart entered the city two years ago, and now has 126 stores in Shanghai.

Traditional Markets: These continue to be a presence throughout China, although they are no longer the dominant factor in the larger cities. Traditional markets fall into three general categories: wet markets, variety stores (xiaomaibu), and fruit stands. Wet markets specialize mainly in fresh vegetables, meat, poultry (sold live), eggs, tofu and to a lesser extent, fruit and staple foods. Sanitary standards are extremely low, particularly for meat. Officials generally regard wet markets as an eyesore, as well as a source of both food safety problems and unregulated (i.e., untaxed) commerce. The SARS epidemic of 2003, followed shortly by avian influenza outbreaks, provided more impetus to efforts to reform or close these markets. Nonetheless, they persist. The main reason for this is a lack of alternatives for buying fresh vegetables and, to a lesser extent, meat. With local government support, however, supermarkets' efforts to expand the fresh section, and especially with consumers' growing concerns over food safety, these traditional markets will gradually be phased out.

The other traditional formats are small variety stores (xiaomaibu) and fruit stands. The typical xiaomaibu is much smaller than even a convenience store, family owned, and stocks an eclectic mix of products. Although they face a serious challenge from convenience stores, the xiaomaibu persists even in Shanghai. While convenience chains follow standard formats and target key sites (train and bus stations, schools, hospitals, etc.), xiaomaibu are infinitely adaptable. Small size and independent ownership allows these shops to adapt to individual sites such as apartment complexes, and adapt their product selection even to match individual consumers. Like convenience stores, xiaomaibu also offer a range of services such as bill payment and IP telecommunication card sales.

Fruit stands fill another gap left by the convenience stores, which rarely carry more than one or two types of fruit. Sales are boosted by the tradition of giving gifts when visiting friends, and most fruit stands will wrap fruit baskets to order. Fruit stands frequently carry imported fruit, usually for inclusion in fruit baskets. However, they are generally regarded

as poor venues for imported products, as they are generally price driven, poorly regulated and lack the means to store fruit properly. Counterfeiting is widespread in these markets, and where a brand name adds value, it is certain to be copied. As a result, there is little room for marketing and promotion of imported products. While both xiaomaibus and fruit stands will likely continue to decline in numbers relative to convenience stores, China's high urban population densities are likely to support their continued existence for many years.

Product Distribution

Retail distribution channels have not grown to match the number and quality of retail outlets. Roughly the size of the continental U.S., China does not have a nationwide network of trucks, highways and cold storage warehouses that can efficiently deliver supplies from the manufacturer or importer to the store shelf. With some notable exceptions, distribution is handled on a store-by-store or city-by-city basis, with stores receiving most imports through a local distributor, often even when alternatives exist.

Because of their relative size, stores are able to negotiate highly favorable terms that include free return of unsold products, high listing fees for new products, and credit terms, effectively passing all market risk onto the distributor. This gives store managers a powerful incentive to favor the local distributor over alternatives that offer less generous terms. In at least one case, an international retailer's effort to establish single-desk distribution of imports failed when their own stores refused to work with the selected distributor.

A second reason for reliance on local distributors is the tendency of international retailers to expand rapidly nationwide rather than focusing on a single city or region, creating large numbers of isolated stores that lack the volume to support a dedicated distribution network. A final reason has to do with the role of relationships in Chinese business: local distributors can provide a store with a network of business and government contacts that are useful in resolving problems with minimal fuss.

Fragmentation among suppliers of locally sourced products, particularly of vegetables and meat, helps to perpetuate the dominant role of the local distributor. This is changing slowly, as the government encourages direct sourcing and farmers' professional associations become more common, giving producers the ability to supply larger quantities

from a single source and at a more consistent level of quality.

International retailers have recognized the problem and put a greater effort into improving the logistics system. Right now, Wal-Mart is focusing on building a nationwide distribution network, and has a recently built distribution center in Tianjin. The German retailer Metro has a centralized distribution system for many imported products, and a few large distributors have negotiated more favorable terms with retail chains at the national level, in some cases waiving listing fees. Carrefour also contracted with a third party logistics company to handle most of its imported grocery items. But fresh and frozen items still rely on importers or distributors to deliver to the stores themselves. The role of the local distributor in handling imports is declining. Nonetheless, for now, distribution remains the key obstacle to sales of imported processed foods in China's retail sector.

Because of the high level of risk they are expected to absorb, distributors tend to be very conservative about new products, particularly imports. As a result, penetration of imported foods into the retail sector is low. Even in relatively affluent cities, international retailers typically carry less than 1% imported SKUs. Notable exceptions include stores in Shanghai, Beijing, Guangzhou and nearby boomtowns, which are home to both large expatriate communities and to a large number of Chinese with overseas experience. Products that are already in the market but being sold mainly through gray channels or sub-distributors tend to be the most attractive to distributors.

Farther inland, distribution problems are complicated by China's heavily fragmented logistics systems, which make it difficult to transport products directly from the coast to deep inland cities. One survey in Chengdu found that temperature sensitive items, such as imported poultry and meat, changed ownership as many as five times before reaching the final user.

A lack of appreciation for the value of maintaining the cold chain creates special problems for temperature sensitive items. Even if cold storage is used at the port of entry and the retailer maintains the appropriate environment, getting drivers to maintain the correct temperature during transportation has proved difficult. While this certainly true in secondary markets, where frozen products often have a frosty covering, is also true in the major coastal markets.

Distributors generally fall into one of two categories. The largest distributors tend to have longstanding relationships with the major retail chains, and can source in larger volumes

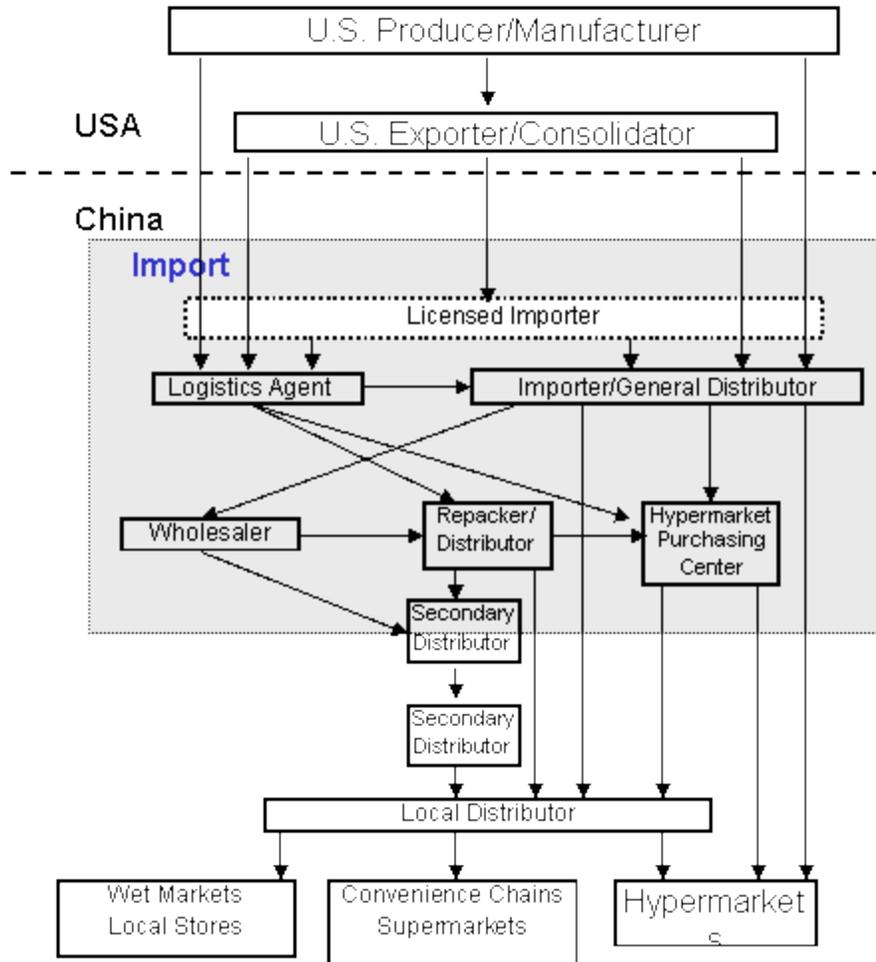
and place products in a larger number of stores. However, they also tend to carry a large number of SKUs, and cannot dedicate resources to marketing any one particular item. Specialty distributors tend to be focused on one area or product type. Although they sometimes lack the volume and connections of larger distributors, they tend to be more aggressive in marketing products and better at identifying and selling into specific niches. The quality of these smaller distributors varies widely, however, and exporters need to be very careful in selecting a partner.

A handful of retailers also act as distributors. Although they tend to provide less marketing support, they can be an effective means of getting product to retailers that have already expressed an interest, but cannot handle the import formalities themselves.

Geographic Differences in Distribution

Distribution varies widely throughout China based on geography, product type and retail sector. As a general rule, the three cities of Shanghai, Guangzhou and Beijing have the best infrastructure and the largest number of experienced distributors. Increasingly, those systems are being extended to the large webs of satellite cities surrounding Guangzhou

Chinese Distribution Channels



Source: ATO/Shanghai research

and Shanghai. Ports in these cities offer a growing array of services, including bonded storage (with temperature controlled facilities, if needed) and online inventory tracking. Some have duty-free industrial zones where products can be repackaged or further processed, with duty paid only on the original import value, and only after products leave the zone.

Other major cities along the eastern seaboard, beyond the reach of the ‘big three,’ generally have good logistics infrastructure, but most still rely on one of the ‘big three’ as an entry point for imports. The number of distributors handling imported products in these cities is usually limited. These tend to be good markets for commodity products such as meat, poultry, fruit and seafood, as well as sauces, condiments and wine.

Farther inland, there are a number of large cities with good market potential. Logistics can be problematic, but improvements in the national highway system have made trucking

direct from Shanghai or Guangzhou far easier than it was just a few years ago. As a result, high value and sensitive products shipped by truck directly from the importer to a local distributor do surprisingly well, while lower value and shelf-stable products that ship on local roads through conventional distribution chains face more difficulties. Distribution in these cities is generally underdeveloped. Many cities have only a single distributor for imports, particularly high-value or temperature-sensitive products. Products going through conventional distribution channels typically change hands numerous times before reaching their final destination. Distribution channels for HRI tend to be better developed, and may be the best place to start for exporters seeking to develop new markets.

Distribution by Product Type

Distribution also varies widely by product type. Channels for shelf-stable grocery products tend to be the most heavily fragmented and the most dependent on the good graces of local distributors. This is partly because market risk is perceived to be higher: although shelf stable, the number of SKUs tends to be high and turnover low compared to other product categories. Hence the risk that a product will not sell (and the distributor will have to accept a return) is higher. Meat, poultry and seafood also face fragmented distribution, but the combined demand from HRI and retail venues is sufficient to warrant special arrangements for these high-value products. Fresh fruit appears to have the best distribution, working through a patchwork of wholesale markets and specialized distributors that works better than it should. Imported frozen corn and mixed vegetables are almost universally available, reinforcing the notion that the problem is less one of logistics than of distribution. Wine deserves special mention, due to the presence of a community of specialized distributors, some of whom act as exporter, importer and distributor all in one, taking product directly to retailers.

New Trends in Retail

Direct sourcing of food and agricultural products from farm cooperatives has been adopted by most retailers in Shanghai and is growing elsewhere. This allows retailers to address consumers' concerns about food safety, reduce cost, and possibly improve product quality. On the imported product side, Wal-Mart started to directly source and import U.S. cherries this year.

Neighborhood Supermarkets were opened in Shanghai by Carrefour and Tesco this year. These outlets offer low prices and fresh food as their selling points. The prices in

Tesco Express are as competitive as in Tesco Hymall (hypermarket). Seventy to eighty percent of the products in Carrefour's trial express neighborhood outlet are also fresh and live food. Making use of Carrefour's purchase and logistics system, its operating cost is much lower. Fresh and live products have become hypermarket's core products and are increasingly important to their sales. These express outlets may turn out to be a way for supermarket to survive the fierce competition from hypermarkets and convenience stores. Such outlets can better cater to consumers' daily needs due to their convenient location. Shanghai Lotus opened a **neighborhood hypermarket** in 2008 which also has fresh food as its core offer.

Private label products are new development in China. Each hypermarket, supermarket and convenience store chain in China has a unique private label offer: Carrefour, Great Value, IKA, Tesco and Lianhua are private label lines from leading players. In terms of imports, more private label products are coming on the market here. Metro has moved ahead of the pack in this regard - it imports salmon from Norway by itself, and then packs it and sells in under its private label brand IKA.

Carrefour's Dia **discount stores** carry many of the same staple goods as supermarkets at discounts, but do not carry fresh products. Import penetration is also very low. While the threat from Dia and Nonggongshang's 5 Reminbi discount stores should not be understated, the concept has not succeeded thus far. The stores are small, carrying a limited range of products, and most of them are located nearby residential areas. The proportion of private label products in the stores is too small however, and some of Dia's products apparently did not appeal to Chinese consumers. The number of 5 Reminbi stores has fallen over the last few years as the concept struggles.

Several **specialty wine retail** outlets have opened in Shanghai. These sell a selection of imported and domestic wines and are not to be confused with state-owned liquor and tobacco stores. The most notable is Napa Reserve, which features a wide range of wines from that region of California. (Please see [CH8802](#) Shanghai_Retail Wine Show.) The Chinese wine market is more completely analyzed in the National Wine Market Report [CH9808](#).

Retailer Profiles

Domestic retailers generally have an advantage over foreign retailers, and China is not an exception to the rule. Lianhua and the Suguo - Vanguard combination are easily the largest

food retailers in China. The three largest multinational chains - RT Mart, Carrefour, and Wal-Mart - have not been in a position to challenge the local incumbents for sales leadership. If you look at the hypermarket channel, or imported products however, the situation is different. Most of the Chinese domestic retailers focus on a clientele that is more representative of the Chinese population than that of the multinational retailers. They also have store base that is often older, partly franchised, and has large numbers of smaller properties.

While the domestic retailers are becoming more interested in imported products, importers have traditionally focused on, and gotten better results from, the multinational hypermarket retailers. The number of hypermarkets by retailer in selected cities and the total number of stores by retailer in Shanghai are presented in the appendix.

The table below gives a snapshot of the relative competitive position of some of China's leading food retailers. The data is for the year ending December 31, 2008. Much has changed since then. Wal-Mart now has more stores than Carrefour, and RT Mart and Auchan seem to be joining forces. The numbers in the following profiles reflect our current understanding.

Leading Food Retailers in China: 2008				
Company	Ownership	Business Line	Stores	Sales* ¥ billion
Chinese				
Lianhua	China SOE**	Super/Hypermarket/ Convenience	3932	74.0
Wumart	China Pvt	Supermarket/ Convenience	726	31.0
Suguo (CRV)	China SOE***	Supermarket/ Convenience	1802	45.0
Nonggongshang	China SOE	Super/Hypermarket/ Convenience	3330	39.0
Vanguard (CRV)	China SOE	Super/Hypermarket/ Convenience	2698	49.1
Xiuyijia (A. Best)	China Pvt	Department	105	25.0
Wuhan Zhongbai	China SOE	Super/Hypermarket	626	16.0
Multinational				

RT Mart	Taiwan	Hypermarket	101	49.4
Carrefour	France	Hypermarket	134	49.7
Wal-Mart	U.S. JV	Hypermarket	123	41.0
Metro	Germany JV	Hypermarket	38	18.5
Tesco	U.K. JV	Hypermarket	61	19.9
Auchan	France	Hypermarket	31	11.9
Lotus	Thailand	Hypermarket/Convenience	76	19.1
* Food and non-food sales			Source: China Chain Store &	
** SOE= State-Owned Enterprise			Franchise Association 2008	
*** Joint venture with China Resources Vanguard				

Hypermarkets

Wal-Mart's presence in China not only includes its Wal-Mart hypermarkets, but **Sam's Club**, and **Trust Mart**. Wal-Mart purchased 35% of Taiwanese owned Trust Mart in 2007, significantly expanding its footprint. *Trust-Mart* would be one of the biggest retailers in China even without its connection to Wal-Mart. This Taiwanese company has over 100 hypermarkets, mostly in eastern and southern China. While Wal-Mart has the option to purchase the remainder of Trust Mart in 2010, recent press reports indicate that Wal-Mart has suspended the merger. However, these reports may reflect negotiations about price by another means. Wal-Mart itself currently has 172 stores in China.

Compared to the other international retailers Wal-Mart may be more willing to open stores in secondary cities and in suburbs rather than directly targeting the higher income central city areas directly. Until recently, Wal-Mart's development in China had been mostly limited to the southeastern seaboard area where household consumption is high. In 2005, Wal-Mart made an entrance into Shanghai with the opening of a large suburban outlet. It has established a second company in Eastern China to manage its expansion in the Shanghai area. Wal-Mart set up its headquarters and opened its first store in Shenzhen in Southern China 13 years ago. Its "Everyday Low-Price" strategy helps Wal-Mart attract traffic, and it continues to aggressively open new stores to penetrate mainland second- and third-tier cities.

In addition to *Wal-Mart* supercenters, *Sam's Club* has gained a good reputation in introducing imported food to local consumers. To date, four *Sam's Clubs* have opened, including one in Shenzhen, one in Panyu, Guangzhou, one in Beijing, and another in Fuzhou. The Shenzhen store is reported to be one of the most profitable *Sam's Club* stores in the world. ATO/Guangzhou, along with several cooperators, is working closely with three *Sam's Clubs* in South China to conduct a regional promotion featuring various snack foods and fresh items.

Carrefour has made great efforts to increase its fresh produce SKUs to the range 3,000 to 5,000 per store. Carrefour currently operates about 156 stores in China, extending even to the far western city of Urumqi. Many of the new stores are or will be located in markets where Carrefour previously lacked a presence. Carrefour's recent overall strategy has been to increase investment and expand into more second tier and or third cities in China, mainly because of an increasingly saturated environment for retail outlets, and rising rental and manpower costs in first tier cities.

While Carrefour continues to dominate at the high end, with 19 hypermarkets presently in Shanghai alone, its single store sales were surpassed by Taiwan-based retailer RT-Mart and Wal-mart now has more stores.

Carrefour China has a new CEO with a finance background. Since his arrival, Carrefour has paid more attention to profitability and has become more conservative in terms of new product sourcing and merchandising. This impacts the introduction of new imported products. Carrefour's internal organizational structure and policy has changed to favor people with a finance background and a volume sales-oriented strategy.

RT-Mart had 102 stores in China, with 10 outlets in Shanghai alone, at the end of 2008. Although overall store numbers lags behind Wal-mart and Carrefour, its single store sales are the highest. It has reached an agreement with French retailer Auchan to set up a joint share-holding company listed in Hong Kong in the near future. Its goal is to pass Carrefour to become the largest sales volume retailer in China.

Auchan has stores in Shanghai, Beijing, and Chengdu. Its customers are largely upper-middle and middle class consumers. Auchan has a centralized system for import distribution. Its purchasing and distribution department are located in Shanghai.

Lotus has a target of 100 stores in the next few years. It has quietly expanded and has 21 stores in Shanghai, although turnover for these stores is lower than for Carrefour stores. Import products have a relatively small presence in its stores compared with the other retailers. And it has changed its marketing slogan from "Everyday Low Price" to "Freshen Your Life", indicating an attempt to stand out from its mass positioning. In terms of imports, it prefers to source directly for any volume-sales products on a consignment

basis, which is relatively harder for U.S. exporters to accept.

AEON-Jusco is a key retailer in Northern and Southern China. It uses a Japanese General Merchandise Store (GMS) approach where the store sells many types of merchandise, including food, fashion, house ware and electronic appliances. AEON Jusco stores have an excellent reputation in southern China for carrying high quality imported foods. Their target customers are mid-to-high income consumers. *Jusco* stores encourage a wide variety of food categories and also cater to the expatriate community in the Pearl River Delta. Store managers in Southern China have been very eager to carry U.S. food and beverage products to meet the demands of their customers. Customer traffic in Shenzhen stores typically exceeds 20,000 shoppers per day. During the past three year, Jusco worked with the *ATO Guangzhou* office to hold American Food Festivals in its Guangdong supermarkets. Each year the sales of U.S. food item increased by 20-30 percent.

In Northern China Jusco opened its first hypermarket in Qingdao in 1998, with 40,000 square meters of retail space and parking for 1,000 cars. The format links shopping with leisure by offering a supermarket, coffee shops, other shopping and restaurants under one roof, and became a top expatriate and middle class Chinese consumer destination. Imported food products account for 6 percent of total food products offered at Jusco and focus on fruit, snack food, beverages and dairy products. Jusco opened a hypermarket in Beijing last year just outside the Fifth Ring Road targeted at high-end consumers from surrounding upscale communities, and auto owners shopping on the weekend. In 2009, the retailer also moved into the convenience store business and currently operates nine convenience stores -- with plans to have 50 by the end of the year.

Metro relies on its niche-market strategy of targeting small and medium sized restaurants, effectively positioning itself as an HRI wholesaler and distancing itself from its competitors. To this end, Metro has added a training kitchen to its facilities in Shanghai. Historically it has opened stores more slowly than other international retailers, but it recently announced plans to open stores at much more aggressive pace. Depending on the opening dates of 4 new stores, Metro may currently have 42 stores throughout China.

Metro has the widest selection of imported products of any of the key retailers, and 10 percent of their sales revenue is from imported products. Metro has a membership system similar to that of Sam's Club or Costco. Their large section of frozen processed foods,

including desserts, frozen vegetable mixes, and frozen potato products, is easy to use and open to U.S. products. Metro's main competition is the local wholesale market, not other high-end hypermarkets.

Its import company previously intended to import volume-sales products directly, but now more focuses on importing its own private label products from Europe. Its import department has been dismantled, and the staff has been re-allocated to product categories departments.

Tesco moved its headquarters to Shanghai in 2009 and has 19 stores in metro Shanghai. It opened a new retailing format in Shanghai in 2008. Called the "Express", it has fresh food as its core offer. Import products SKUs are relatively higher at Tesco than Lotus, but Tesco still lags behind Carrefour.

China Resources Vanguard (CRV) is one of the leading retail chain operators in China. This HK based operator manages hypermarkets, supercenters and superstores under the *Vanguard* brand name. Its first store was opened in Hong Kong in 1984, and it entered the supermarket business in Shenzhen in 1991, Suzhou in 1995 and Beijing in 1998. Acquisition helped *CR Vanguard* become national number one retailer in terms of number of outlets and total sales. It acquired "Suguo" supermarket in 2004, and then purchased Tianjin "Yuetan" in 2005 and "Jia shijie" in 2007. In 2008, CRV completed the acquisition of "Aijia" supermarket in Xian. This year, CRV entered Wuxi by acquiring 100 percent stake of "Yongan" supermarket.

By the end of 2008, CRV had 2,700 stores (up 248 from 2007 figure) in China. This includes 200 hypermarkets and 2,306 supermarkets as well as over 80 community stores and 12 *Ole* stores. The total sales reached US\$9.4 billion. Generally speaking, *Vanguard* targets customers likely to buy local produce; however increasingly, higher income shoppers are beginning to show interest in high-quality U.S. imported foods. In some selected stores, special imported food section has been opened to promote imported food items. *Ole* stores are discussed further in the Specialty Supermarket section below.

Century Lianhua is the hypermarket brand of the state owned Balian group. This group's food retail side is dominated by supermarkets, but it has substantial number of hypermarkets in East China. While it is still small, they are focusing on improving their selection of imported products in both Hangzhou and Shanghai. In Shanghai they are also starting to import directly.

Department Stores

Ito Yokado and **Isetan** are high-end, Japanese-owned stores that target upper class consumers. These retailers' emphasis on expansion in to these second-tier markets suggests that there is easier access for high-end retailers in the second-tier markets. China wide, Ito Yokado has two stores in Beijing and one store in Chengdu. Isetan's Chinese stores are in Shanghai and the second-tier cities of Jinan, Tianjin, Chengdu, and Shenyang. Depending on the market, higher end grocery stores in a department store may carry a large selection of imported products, or a section of a store that specializes in other types of merchandise may be dedicated to imported dry goods. There are many other examples of department stores containing a high end grocery store or supermarket.

Specialty Supermarkets and Boutique Stores

Jenny Lou's is a major retailer of imported food products for expatriates, upper-middle income Chinese consumers and others who have lived or studies overseas. The company was established in 1995 and operates 12 supermarkets in Beijing located in high-income and/or upscale communities – often near diplomatic compounds and missions. More than 98 percent of the products offered in the small supermarkets are from overseas -- with more than half from the United States. In particular, breakfast cereal, seasonings, dairy products and wine make up the greatest focus of offerings. Jenny Lou reports that the economic downturn had some impact its business with sales down between 5-10 percent. The store has been affected by the departure of expatriate workers and customers trading down to less expensive products.

City Shop sells an extensive range of imported foods. Over 85% of City Shop's products are imported, and City Shop carries nearly 3,000 American food and non-food products. Started as a corner shop by a former Cochran fellow, City Shop now has 9 retail outlets in Shanghai and one in Beijing. It has developed its own system of retail and wholesale services. It maintains its own farms with internationally recognized organic farming and logistics systems. It produces 140 different organic vegetables and herbs, and produce is transported daily via temperature-controlled trucks to City Shop outlets and other wholesale business partners.

Ole, operated by CRV, targets upper-middle income shoppers and white-collar workers. Its 10 Beijing stores are all located in business or shopping centers. There are two stores in Shenzhen, with another set to open in Guangzhou. Another new store located in the China World Phase III in Beijing is scheduled to open at the end of 2009. Imported food product sales are approximately 50 percent or more of total food sales. The stores in Shenzhen have been successful in introducing imported foods such as cheeses, chocolates, coffee, wine, liquor, biscuits and fresh fruits at higher prices. Undermining this early success is an unstable supply chain and lack of promotion to support further demand growth. Ole is reportedly planning to open Shanghai stores in the near future.

Supermarkets

Lianhua, Hualian and Nonggongshang are three large state owned supermarket chains. These, and other domestic firms, dominate the supermarket sector. Although Lianhua and Hualian were nominally merged three years ago to form the behemoth Bailian, the largest retailer group in China, they continue to operate as distinct (and competitive) chains. Bailian appears to be more focused on rationalizing its diverse portfolio, and developing its shopping mall management component. Both Lianhua and Hualian have expanded aggressively through acquisitions of other chains, leaving both companies with the challenge of incorporating them into already weak state owned management structures. Inspired by foreign-invested companies, the Chinese chains are paying greater attention to branding, and most now carry a substantial number of house brands.

All three have also opened branded hypermarkets in and beyond Shanghai, and Lianhua is putting a particularly strong effort into its Century Lianhua hypermarkets. Although Nonggongshang's market share has slipped, it is attempting to expand its reach to match Lianhua and Hualian, opening NGS hypermarkets in distant cities like Nanchang, with mixed results.

The state owned supermarket chains also play another role – that of the local partner of international retailers. The international players had to agree to this to enter China. So Lianhua, for example, owns a large minority position in both Carrefour and Metro.

China Resources Vanguard also has a large number of supermarkets. It acquired with Suguo, a regional giant headquartered in Nanjing in 2004. The brands continue to operate independently.

Wu-Mart is a major retail chain based in Beijing that operates more than 2,000 stores throughout China featuring hypermarkets, supermarkets, and convenience stores targeting middle class and low end consumers. Retail sales reached \$4.4 billion in 2008 based on expansion and acquisition. In 2005, Wu-Mart acquired a 25 percent share of Beijing Mei Lian Mei to increase its market presence in Beijing. Wu-Mart also acquired a position in Xin Hua Bai Huo in Yin Chuan and Zhejiang Gong Xiao in 2008 to expand its number of outlets significantly throughout China.

Advantages and Challenges for U.S. Products

Overall, U.S. products enjoy a high image in the China market. Rising incomes and growing concerns over food safety among Chinese consumers after numerous episodes of food contamination mean there will be more opportunities for U.S. products, which are largely perceived as safe and wholesome. On the other hand, price is still one of the barriers for U.S. products to reach more Chinese consumers; other challenges include labeling regulations, distribution, and limited product knowledge. The following table provides further details.

Advantages and Challenges for U.S. Products	
Advantages	Challenges
U.S. products are regarded as high in quality, and manufactured with high safety standards.	Many U.S. products are costlier than their local counterparts.
Urban Chinese consumers spend 36% of their income on food.	Overall incomes remain relatively low, with imports selling mainly to higher income groups.
Consumers are interested in new tastes.	Consumers are very price sensitive, and often unwilling to risk spending money on unfamiliar products without trying them first.
Many U.S. brands are widely recognized and respected in China's major urban markets.	Many U.S. companies have established plants in China, manufacturing their products in China with Chinese ingredients.
Incomes are growing rapidly in second and third tier cities, creating a whole new range of opportunities.	Distribution and logistics remain underdeveloped outside of the largest urban centers, making distribution of imported products to interior cities difficult.
Western foods are more widely available than ever, and growing in popularity with consumers.	Lack of knowledge about U.S. products and how to prepare them properly makes consumers hesitant to buy.
China's entry into the WTO reduced tariffs on a wide range of imported products.	Labeling regulations and sanitary restrictions limit access to the market. Enforcement of regulations is haphazard, creating confusion for exporters.
The number of qualified distributors for imported food on the mainland is	Many U.S. exporters continue to rely on gray market channels, reducing their level of contact with end users

growing, along with the volume of direct exports.	and understanding of the market.
Rapid growth in retail chains has created the potential for bulk sales, with consequent improvement in pricing and handling.	Purchasing by most foreign-invested chains remains decentralized, preventing them from sourcing in bulk. Close relationships between store managers and local distributors help to reinforce this tendency.

Competition and Best Prospects

The most serious competition for U.S. food exporters comes from local and joint venture food producers and processors. The quality of fruit and vegetables in particular has increased rapidly, and many local traders now contend that the best of China's fruit is similar in quality to imports. The general lack of coherent marketing systems continues to plague China's industry, however, making it difficult to source significant quantities of products with consistent quality. While oranges similar in quality to U.S. navel oranges are available, the transaction costs of dealing with large numbers of small farmers, then sorting and packing raises the final market price to levels similar to imports. The formation of farmers' voluntary organizations such as the Zhejiang Pear Association has the potential to reduce these problems, but such organizations are still relatively new.

Competition is equally intense for processed foods, although differences in taste mean that the primary competition comes from third country competitors or joint venture manufacturers. Shelves may appear to be stocked with famous foreign brands such as Kraft, Lays and M&Ms, but close inspection reveals that most of these products are manufactured locally or in Southeast Asia. This allows manufacturers to cash in on brand identification, take advantage of low labor costs in China, and adapt their products to Chinese tastes and labeling regulations, all at the same time. Years of food adulteration scandals have made Chinese consumers cynical, however, and most will attribute a higher level of quality safeguards to food products that are genuinely imported.

The general trend to date has been for local manufacturers to push imports out of the price-driven mass market and into niche markets where quality and novelty are more important than price. This has already happened to varying degrees with pet food (Mars' locally manufactured Pedigree and Whiskas labels dominate the middle market), wine (Chinese labels dominate at the low end), apples (Washington State apples sell extremely well in gift markets) and confectionery (Mars). Growing local competition has emerged for table grapes, and domestic sweet cherries, lemons and almonds appear to be improving in both

volume and quality, albeit from a very low base. Certain products, particularly western-style prepared foods, face little or no competition from local manufacturers, constituting a niche unto themselves. Improvements in quality and increased efforts at brand development are allowing Chinese companies to compete more effectively for some niche markets, but local manufacturers face the same distribution problems as imported products, as well as a high level of skepticism among consumers.

Third country competition comes in two distinct areas: commodity-type products such as frozen meat, poultry, seafood and fresh fruit, and western-style niche products such as canned and prepared foods and ethnic cuisines and ingredients. Competition in the fresh and frozen meat, fruit and vegetables arena, as well as dairy, comes primarily from Pacific rim neighbors, including Thailand, New Zealand, Australia, Canada and Chile, as well as South Africa and Brazil. Competition for western-style prepared foods is much more global, with competitors playing to their strengths in individual products such as olive oil, wine, pasta and pasta sauces.

The U.S. remains the largest single exporter of consumer-oriented food to China, and is the only exporter with a presence in most categories. China is attracting a growing level of interest from other countries, however, and has signed or is negotiating bilateral trade pacts with many of its neighbors. The following is a brief outline of key products and competitors.

Key Products and Competitors

Selected U.S. Imported Products	Main Foreign Competitors
Red Meat	Canada, Denmark, New Zealand, Australia
Poultry: chicken paws & wing tips	Brazil, Argentina
Oranges	New Zealand, South Africa
California Table Grapes	Chile
Washington Apples	Chile, New Zealand
Cherries	New Zealand
Breakfast Cereal	United Kingdom, Australia, EU
Cheese and Dairy	New Zealand, Australia, EU
Frozen Processed Products	Canada, New Zealand
Wine	Australia, France, Italy, Spain, Chile

Spaghetti sauce/tomato products	Italy, France, EU
Coffee	Japan, France, South Africa
Candy and Chocolate	Switzerland, Italy, France, Belgium, Japan
Nuts	Iran (pistachios), Mongolia, Korea (chestnuts) Russia
Seafood	Russia, North Korea, Canada, Norway, Japan
Ginseng	Canada, Korea
Dried fruit: prunes and raisins	France and Italy (prunes)
Baby food/infant formula	New Zealand, Switzerland
Premium Ice Cream	France, New Zealand

Best Prospects

Products Present in the Market Which Have Good Sales Potential

- Nuts and dried fruit (prunes, raisins)
- Seafood
- Poultry meat
- Red meat (U.S. beef and related products are currently not permitted entry into China)
- Frozen vegetables (esp. sweet corn)
- Infant formula
- Baby food
- Dairy products (cheese and butter)
- Baking ingredients and bread bases
- Frozen potato products
- Fresh fruit (oranges, apples)
- Premium ice cream

Products Not Present in Significant Quantities, Which Have Good Sales Potential

- Fresh fruit (cherries, pears)
- Processed/dried fruit (blueberries, cranberries)
- Mexican, Indian food
- Ready-to-cook and ready-to-eat foods
- Organic foods (niche market)
- Functional foods

Guidelines for Entering the Market

China is not a single amorphous market, but a jigsaw puzzle of small, overlapping markets separated by geography, culture, cuisine, demographics and dialects. As such, there is no single formula for success in China. The best approach to marketing a product will vary depending on the product and the specific market (geographic and demographic) being targeted. Nonetheless, there are some basic guidelines that can be applied to most cases.

1) Understand the importance of relationships. China's legal system is developing, but remains inconsistent. Enforceability of contracts varies widely, but is generally weak. Business in China instead relies heavily on personal contacts and influence (referred to as 'guanxi'). For companies with a serious interest in China, no investment will be more important to their success than the network of relationships that they establish in China. For more pointers on the role of guanxi in Chinese business culture, please see report [CH4835](#), Chinese Business Etiquette.

2) Find a local partner and/or distributor. For smaller companies without the resources to directly market their products in China, a good distributor is critical to success. Distributors provide the network of relationships with buyers, regulators and others, that is essential to doing business in China. Unfortunately, these tend to be in short supply. ATOs keep lists of well-known distributors. Keep in mind that contract arrangements with retailers tend to place most of the market risk for new products onto the distributor, so they may require some convincing before they will take on an unfamiliar product. Specialized distributors also exist for certain product categories, most notably wine, seafood and fruit. Be careful in selecting a partner and in establishing an incentive

structure: partnerships gone sour are the most common cause of business failure in China. Paying close attention to payment terms can be an important aspect of this (confirmed letters of credit are standard).

3) Know the rules. Chinese regulations are often vaguely worded, arbitrarily enforced and opaque. Your distributor can (and should) handle this for you. However, weak enforcement has made short-cutting a common practice, and exporters that rely entirely on Chinese partners for this are often unaware that their products do not conform to the rules until a problem arises. To defend against the unexpected, exporters should try to be reasonably familiar the actual regulations. Product registration, labeling and product expiry dates are the top concerns in this area. To enter the retail market, food products must receive a hygiene certificate from the local government where the product will be sold. Food products must also be labeled in accordance to Chinese government standards, with the labels pre-approved by the government. Functional or health foods must obtain a health-food certificate, and claims of health benefits on packaging or in advertising are strictly regulated. Foods containing GMO ingredients may be subject to additional labeling requirements, as are organics. There are also a wide range of concerns related to China's new Food Safety Law. Please see the FAS FAIRS reports for China on the FAS website for details (www.FAS.USDA.gov; attache reports) or the website for China's Administration for Quality Standards, Inspection and Quarantine (AQSIQ) at www.AQSIQ.gov.cn.

4) Get to know the market. As noted above, China is a surprisingly diverse place. Tastes, customs, culture, business practices and government regulations vary from place to place. Experience in other markets will not necessarily help in China, and some aspects of the market need to be witnessed to be fully understood. The best strategy is to target a specific place and get to know it well. The scope of your effort will determine whether you select a single city or a whole region. Travel to China is highly recommended to evaluate partnerships, build *guanxi* (see above), and identify new opportunities and potential obstacles. (Partners are frequently hesitant to mention problems in formal communications, but will be more forthcoming over informal events like dinners). FAS market briefs offer a good source of information on the market, and are available for free on the FAS website noted above.

5) Find your market niche and focus on it. China is a very, very big place. The mass market may be huge, but it is driven entirely by price and dominated by lowest-cost local

producers. Better returns are to be had from targeting a specific niche. The country has a nearly infinite number of niche markets, some of them quite large. Examples include the high-end gift market, where margins are high but packaging is crucial (wine, ginseng); the expatriate market (famous brands from home like Kraft, Betty Crocker and Post); or health-conscious young parents (prunes, almonds, fresh fruit).

6) Invest (wisely) in consumer research. To outsiders, Chinese tastes can seem fickle. Tastes poorly received in the U.S. may prove successful in China, while products targeted to one market niche may end up finding their greatest success in a completely different one. To avoid unpleasant surprises and find new opportunities, exporters with a long-term interest in China are advised to research the market and test new products directly. Be careful how you invest research money, however. The quality of research by international market research firms is often not much better than that of much less expensive local companies. ATO-sponsored activities offer good opportunities to field test new products or packaging.

7) Adapt your products. Exporters should be prepared to adapt their products to the demands of their Chinese consumers. This includes flavors, packaging, prices and labeling. Small changes to flavors or packaging, based on market research, may make the product more viable in China. For example, Chinese consumers are often unwilling to buy unfamiliar products if they can't actually see them, so including a transparent window in the box or offering free samples can help sales. Products that are marketed as gifts, such as wine, should place extra emphasis on the packaging, as this is considered an important part of any gift. Many exporters seeking to break into the gift market have special packages manufactured in China, which can also help to address labeling issues.

8) Be flexible. Things don't always work as expected in China. This can be a good thing, provided you can take advantage of opportunities when they arise. Exporters who enter the market with preconceived notions of how to market their products often miss out. ATO activities routinely turn up unexpected opportunities: for premium boneless pork in Chengdu; for d'anjou pears and cherries in Shanghai; for Mexican food in Wuhan. By the same token, a product may find its best niche in an unexpected place. Washington State apples have done quite well in China despite tough competition from local products, because superior appearance and consistent quality made them the top choice for gift baskets.

9) Pursue gradual but sustainable growth. A common pitfall is the temptation to pursue explosive growth, focusing on geographic penetration rather than sustainability. This may produce impressive short-term results, but exporters with limited means may find themselves overextended very quickly. If the exporter is unable to meet the expectations of their customers, they may turn to other sources (such as local copycats or counterfeiters) or demand may collapse. Alternatively, the exporter may find themselves overly reliant on local agents that they do not know well, and who have little interest in the long-term success of the product. The go-slow approach gives exporters time to learn the markets, accumulate customer feedback, and build their distribution channels.

10) Invest in market promotion. Once in the market, an exporter's product will be competing with tens, if not hundreds, of similar products. Domestically made products will often have advantages on price, familiarity and local brand recognition, while imports can be aided by aggressive promotional campaigns. Lacking the massive marketing budgets of multinationals like Nestle or Kraft, most exporters must design and implement their marketing campaigns carefully. Attending only quality, focused trade shows for your particular market segment is a good way to start. In-store promotions are also a cost-effective way to support your product and build relationships with distributors and retailers. Above-the-line media advertising should be carefully planned, as TV and radio time is expensive and has limited reach. Exporters are strongly advised to explore joint marketing opportunities with ATOs or with a State and Regional Trade Groups (such as MIATCO, WUSATA, Food Export USA/NE, or SUSTA). These events tend to be cost effective and draw more attention than stand-alone promotions.

Regional Profiles

China is a diverse place, and fragmented distribution and logistics systems help to reinforce existing divisions. To assist exporters in dealing with these regional differences, FAS maintains six offices in China, with Agricultural Trade Offices (ATO) in Beijing, Shanghai, Guangzhou, Chengdu and Shenyang , and an Agricultural Affairs Office in Beijing. Individual market profiles for each region are offered in the following sections, written by the respective ATO offices.



Eastern China - Shanghai and Yangtze River Delta

The city of Shanghai is a massive market unto itself, with a population estimated at 20 million, and incomes among the highest anywhere in China. As costs in the city have risen, the economy has begun to shift away from manufacturing and into financial and management services. Manufacturers seeking to escape high costs in the city while taking advantage of the infrastructure and massive consumer base have created an economic boom in the surrounding region. The city is located at the center of a web of economic development that includes the provinces of Zhejiang and Jiangsu, and is collectively referred to as the Yangtze River Delta (YRD). This region accounts for nearly 1/3 of mainland China's GDP. Massive infrastructure investment has led to major improvements in logistics and drawn the region closer together. The opening of the Yangshan deepwater port facility is expected to make Shanghai the world's largest container port within the next few years. Shanghai's large expatriate community (estimated at 500,000) is dominated by Taiwanese, who bring with them a familiarity with foreign brands and a taste for U.S. and Japanese foods.

Shanghai's retail sector is increasingly saturated, and home to a large number of supermarkets, hypermarkets and an extremely strong convenience store sector.

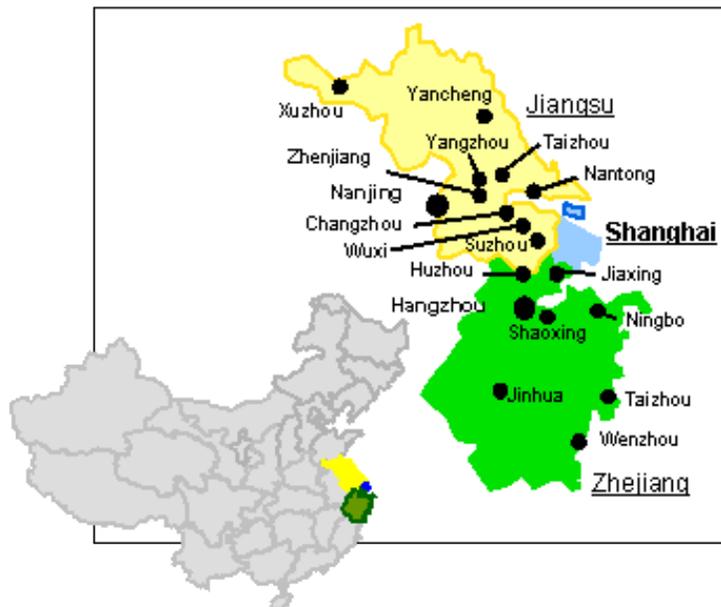
Supermarkets remain the dominant, and oldest, modern retail format, with relatively weak management and infrastructure. Supermarkets are losing ground to hypermarkets and convenience stores. This loss in market share, however, is counted in growth not captured; new stores continue to open. The supermarket format is quite durable owing in part to Shanghai's high population density (the highest in China and one of the highest in all of Asia), which makes it possible to have a small supermarket within walking distance of virtually any place in the city.

Influenced by the global financial crisis, economic development in Shanghai slowed down in 2008, but GDP still grew by over 9% in real terms. Stimulating domestic demand is one of the Chinese government's measures to combat the economic downturn. Overall, retailing in Shanghai still remains robust and retailers are working on new concepts to lure consumers, such as market segmentation, so as to produce points of differentiation and create an edge over competition.

Beyond Shanghai

The immediate area surrounding Shanghai (the Yangtze River Delta, or YRD) is a beehive of industrial and commercial activity. In the key cities, retail development is already well advanced. Suzhou and Hangzhou are home to Carrefour and other hypermarkets, as well as convenience stores. Hypermarkets throughout the region source imports through Shanghai, taking advantage of the region's outstanding logistics and Shanghai's large

The Yangtze River Delta



community of experienced food importers. The supermarket sector in these cities is typically dominated by either Lianhua, Hualian or Nongongshang, but with a preponderance of independents (with the notable exception of Nanjing's Suguo).

The capital of Zhejiang Province, **Hangzhou** is home to Carrefour, Metro, Lotus, Auchan, Wal-Mart, Lianhua, and Hymall, among other super- and hypermarkets. Hangzhou's retail market is doing far better than expectations: in an ATO-organized nationwide retail promotion involving 24 Carrefour stores, the Hangzhou store ranked 7th in sales: ahead of Guangzhou and following stores only in Shanghai (4 stores) and Beijing (2 stores). In addition, the Hangzhou store was extremely aggressive in recruiting distributors and products for the event, and ultimately carried far more items than originally agreed. (Please see [CH7819](#)). In a departure for a state owned chain, Lianhua is actively promoting imported products in Hangzhou and plans to open a specialty supermarket concentrating on imported products.

Suzhou's market is steadily growing, and a privately-owned cold chain already exists, with temperature-controlled warehouses and delivery trucks. Metro has established itself in Suzhou as the destination for one-stop shopping, and its membership is already 130,000 strong. To further stimulate market growth, the city's infrastructure is developing at light speed. Several new highways were built recently; bridges cross the Yangtze River, and a light rail system has been scheduled for completion in 2008. (Please see [CH7816](#)).

Development is now moving on to a third tier of cities. Particularly notable are **Wuxi**, which has become a major distribution center for seafood and meat products in the YRD area (see the recent report [CH8806](#) for more information); **Ningbo**, which has average incomes on par with Shanghai but a less well-developed retail sector; and **Nanjing**, the capital of Jiangsu province.

Nanjing's market and imported product consumption have increased substantially. In ATO/Shanghai interviews, major retailers including Metro, Walmart and Carrefour stated that the higher the percentage of imported food items in their store, the better their sales - indicating the high potential for imported food in Nanjing. Nanjing is also home to Suguo, a retail giant that holds more than fifty percent of the city's market.

Although **Wenzhou** is one of the richest cities in China, its market for foreign imports is still relatively underdeveloped. Wenzhou was only opened to international retail giants in 2006. While the market was slow to open, the retail sector is growing quickly. According

to the Wenzhou Retail Association, a “Sourcing Alliance” consisting of all the important retailers in Wenzhou was organized in 2008 to consolidate the sourcing of imported food products, to strengthen the bargaining power of Wenzhou retailers against food importers. (Please see [CH7814](#)).

Wuhan, in Hubei province offers a mid-range prospect. It has a reasonably well-developed retail sector, with Metro, Carrefour and Wal-Mart all represented. As income levels rise throughout urban areas in China, potential markets are emerging in growing cities everywhere. In 2007, 08, and 09 ATO Shanghai has conducted multilevel campaigns to promote U.S. food products in Wuhan. All these events have exceeded our expectations, and we have succeeded in introducing several hundred SKUs to consumers in Wuhan. The city seems receptive to American products, and with the rapid increase of supermarkets, hypermarkets and convenience stores, as well as more than 40,000 restaurants, it has a reasonably developed retail sector. (Please see [CH7815](#), and [CH9801](#).)

Wal-Mart’s remarkable success in **Nanchang**, the capital of Jiangxi province, provides a good case study for retail in China. Nanchang was not generally regarded as a retail market in the same class as Kunming or Chengdu. However, close cooperation with local officials netted Wal-Mart a prime location, just as the city launched a major redevelopment effort, making for a major success. The success of this venture is all the more striking given the relatively weak performance of Nonggongshang’s NGS hypermarket, established several years earlier in the same city, and demonstrates the value of local market knowledge.

Beijing and Northern China

Although expansion is slower compared with recent years, the northern China retail market continues to grow despite the current global economic slowdown. The sector slowed most sharply from the Fourth Quarter 2008 to the First Quarter 2009. However, since the Second Quarter 2009, retail sales have strengthened. The economic had its greatest effect in Beijing and to a lesser extent to coastal cities, while the inland regions of northern China reported little impact.

The economy did shift demand – with high-priced food products more affected by poor as consumers shifted to lower-mid priced substitutes. For example, in Beijing wine priced

under RMB 100 (\$14.62) remained very popular while products above RMB 100 (\$14.62) faced diminished sales. In Tianjin, a reduction in group purchases hit imported fruit sales during the last Chinese Spring Festival. The slowdown on the coast has also reduced eating out, shifting consumption to the home. For example, fresh food products sales in North China have shown positive growth because fewer consumers dine out.

The government stimulus plan, falling rents and lower wage pressure have encouraged both multinational and local retailers to expand operations in northern China – with some even accelerating plans to open stores in 2009. At the same time, intense competition and escalating costs in Beijing have also fueled growth outside the capital. Retailers are increasingly focusing on second-tier emerging cities, particularly richer coastal locations such as Qingdao, Weihai, and Yantai. ATO Beijing expects these trends to continue or even accelerate in the years ahead.

Beijing consumers continue to shift their shopping from “wet” or open air markets to supermarkets and convenience stores with retail consumer sales totaling \$65.7 billion or 20 percent over 2007. Competition is extremely intense in Beijing because local consumers demand diverse and high quality food at competitive prices. As a result of rising costs and standards, some retailers have gone out of business. For example, last December one supermarket located in one of Beijing’s most upscale shopping malls “The Place” literally disappeared overnight.

International hypermarket operators active in Beijing include Carrefour, Wal-Mart, Tesco and Metro. Wal-Mart has followed a strategy of staying out of downtown to avoid direct competition and instead opened new outlets in suburban Beijing in 2008. In order to lure customers, most hypermarkets provide free parking and shuttle bus services adjacent to shopping and entertainment complexes. Special aisles dedicated to imported food products are often arranged by country of origin. A large variety of imported foods such as cheese, butter, and other dairy products, cereal, cookies, coffee, candy, beverages, wine and snack food are represented in such supermarkets. Products come from a diversity of origins with the United States, Spain, Germany, Switzerland, France, Canada, Italy, Australia, and Korea the most dominant. Carrefour and Wal-Mart have lowered prices on selected products by as much as 20-30 percent in Beijing during the New Year and Spring Festival holidays to encourage sales that often continue even after the holidays have ended. Price cutting will likely return as the holidays come again.

Customers in **Qingdao** have shifted from wet markets to supermarkets because of a booming economy and high per capita GDP. Although the retail market stumbled between the Fourth Quarter of 2008 and First Quarter of 2009, it has recovered from the Second Quarter of 2009 onward. The short downturn came because of low consumer confidence. The downtown location of Jusco and Carrefour in Qingdao keeps these outlets busy even during office hours. The leading second-tier city in northern China the market attracted major multinational and domestic retailers. Hypermarkets are popular with the Carrefour only ten minutes away on foot from Jusco resulting in significant competition between these two retail giants. Hisense Plaza opened just before the 2008 Olympic Games and featured a variety of luxury brand goods such as Cartier, Gucci and Louis Vinton targeted at high-end customers in Qingdao and Shandong Province. Hisense Supermarket cooperated with ATO Beijing in holding a U.S. Food Promotion in July 2009 showcasing over 600SKUs of new seafood, dairy, snack foods, fruit and pet food products. Partially because of the event, Hisense Plaza is now known as a top destination to source high quality American Food Products in Qingdao. Marine City, a new giant shopping mall facing the sea, is five minutes on foot from the Hisense Plaza will open in November 2009, including a supermarket with more than 6,000 sqm targeted at upper middle class customers.

Tianjin's median income is much lower than Beijing and Shanghai with consumers very sensitive about price. Carrefour has focused on attracting shoppers by offering lower prices compared with wet markets. Imported products are limited to the downtown area in stores such as Carrefour, Lotus and CRC. Imported products generally do better in the Binhai New Area because of the large number of white-collar workers employed by multinational companies and the large number of expatriates living there. In addition, E-Mart of Korea entered into a joint venture with Tianjin TEDA and has five supermarkets targeting upper middle class customers and Korean expats. Tianjin is an export port, it was hit harder than most by the financial crisis in 2009. Official sales figures do not show this because major retailers persuaded suppliers to take back their products.

Zhengzhou - Based on geographical location and its advantage as a major rail hub and large population, the retail base developed rapidly in this major inland urban center. Young consumers in the city are curious to try new products especially imported food products -- even if their incomes are lower than peers in Beijing and Qingdao. At this point, this curiosity has not yet resulted in a long-term market for imported food products although this seems to be poised to change very soon. Packaged food, fresh fruit,

beverages, beer and wine are the main imported food products with imported dairy, meat and seafood rare in the market. Organic products are scarce in the market given high prices and a lack of awareness. Group purchasing is the primary channel to sell imported food products. In addition, Zhengzhou is also a distribution center for imported foods to inland second and third tier cities in surrounding provinces given its convenient transportation links.

Xi'an, the capital of Shaanxi province is considered the gateway to northwestern China. Over the last 4-5 years, the retail sector has developed rapidly -- from 2004 to 2009, the total number of hypermarket grew from 25 to 63. China Resources Vanguard (CRV) is dominates the hyper market sector in Xi'an with 22 stores. The highest end store is Century Jinhua, which runs five department stores in Xi'an and offers the most diversified imported products in Xi'an.

The coastal resort of **Weihai** with its booming economy attracted the attention of retail investment and has become the next battleground for Chinese retailers. Korean food products are very popular because of the more than 40,000 Korean Expats which has changed the way people shop and eat. The local government has also encouraged foreign investment -- with Jusco, Lotte and Mix City hypermarkets entering the market within 2 km of downtown. Carrefour and Wal-Mart are also looking for new locations downtown as well.

Guangdong and Southern China

South China has an official population in 2007 of 250 million or 19 percent of China's population. South China is almost twice as big as California, but has 7 times the population. By contrast, South China's GDP of \$ 8.3 trillion was about a third of California's. In 2007, Guangdong had the highest GDP at US\$457.2 billion of any single province in China (up 14.7 percent from the previous year) with retail sales valued at over US\$155.9 billion, up 29 percent on 2006 figures. Food consumption accounted for 35.2 percent of Southern consumers' total expenditure.

Although the slow economy in 2008 impacted many regions, food retail sector in South China did not feel the brunt. The Guangdong government tried to stimulate in-country consumption. Guangzhou's territory expands, as several small cities such as Panyu and Zengchen are folded in. Recently, Guangzhou and Foshan municipal governments

encouraged “Same city partnership” project (cooperation in various aspects such as transportation, service, culture, technology and finance etc.) which is expected to help stimulate trade. Economic ties between Fujian and Taiwan have strengthened, this helps Fujian weather the economic storm.

2010 Guangzhou Asian Games (always use the official title) will be held in Guangzhou next November. Substantial investments on construction and infrastructure such as ports and railways are underway. This helps facilitate trade as well as retail businesses. Guangzhou port becomes the third port in China to exceed 10 million TEUs in annual capacity, after Shanghai and Shenzhen. This year, The *Hong Kong-Zhuhai-Macau Bridge* project also kicked off. Upon completion, increased traffic will spur consumption and promotion of imported food in Guangdong province. Cold chain logistics have quickly developed. Training has been given to distributors and retailers.

Higher disposable incomes and continued urbanization have led to a more diverse diet and greater consumer receptiveness to imported foods. South China plays an important role in marketing imported nuts, pistachios, walnuts, candies, juices, wine, dairy, condiments, as well as fresh deciduous fruits, especially imported apples, oranges and table grapes. U.S. cherries have gained ground in recent years. Well off consumers in wealthy, urban cities are less price sensitive than others. These consumers also pay closer attention to food characteristics and presentation such as flavor, freshness, color, and appearance. Gift-giving becomes a fashion, not only during Chinese holidays but also for special events. It

is noteworthy that gift-packaged fresh fruits are also available on retail shelves. Private label and special package design have become popular.

Key consumption markets in Guangdong for U.S. imported food are in **Guangzhou** and **Shenzhen**. Many retailers have already set up stores in satellite cities around Shenzhen such as in **Longgang and Nanshan district**. Supermarkets continue to be the most common retail format, but hypermarkets are gaining in popularity and present in most medium and large-sized cities.

Emerging markets include cities in the Pearl River Delta such as **Dongguan, Foshan, Zhuhai, Zhongshan, Huiyang as well as Zhanjian and Shantou** in Guangdong. In nearby provinces such as Fujian and Hunan, **Fuzhou, Xiamen and Changsha** are also seen as attractive locations for retailers. In the near future, **Quanzhou, Zhangzhou, Jinjiang** in Fujian, and **Loudi, Yueyang** in Hunan are high potential markets.

Dongguan is a key manufacturing base in South China. In the past 20 years, Dongguan has held a steady annual growth rate of 20 percent and is known as China's economic powerhouse with foreign investments. It has gained a large number of expats and well-to-do residents. Dongguan is 56 miles north of Shenzhen (and Hong Kong), 31 miles south of Guangzhou, 47 nautical miles to Hong Kong and 48 nautical miles to Macau. Its transportation systems connect to five ports, Shenzhen-Guangzhou railways and inter-town freeways. The city occupies 952 square miles with a population of 1.7 million locals and 5.24 million migrant workers from all parts of China. It becomes an important market. Both multinational and domestic retailers are fighting to capture the best commercial sites and gain market share. In Dongguan, there are four *Wal-Mart*, three *Trust-Mart*, three *Carrefour*, four *Tesco*, one *Metro* and *Jusco* each as well as eight *CR-Vanguard* stores. More new stores are set to open.

Fuzhou is the capital city of Fujian province. It has over 2,200 years' history and is the hometown for many overseas Chinese living abroad. This gateway to Taiwan attracted substantial investment and plays an important role in cross-strait trade. As an important port city, it has ambitious expansion plans for infrastructure and logistic development. It is estimated that 80 percent of the Taiwanese are Fujian decedents. Fuzhou is one of the key markets for imported foods as many people have relatives living abroad and are more open to a western life-style. Food consumption expenses in 2007 increased 15.6 percent compared with 2006: expenses on meat items increased 25.9 percent while the expenses on fishery, dairy and fruits remained stable, each rose over 10 percent. Existing key retailers in Fuzhou include three *Wal-Marts*, one *Sam's Club*, two *Carrefours* and one *Metro*. *Carrefour* was the first to open with two supermarkets in Fuzhou. *Wal-Mart* opened its first Fuzhou store about 10 years ago and then opened two more stores and one *Sam's Club*. *Metro* also selected Fuzhou to open its first store in South China. All carry imported food items, especially imported fruits from all over the world. U.S. Washington apples, seedless table grapes, Sunkist oranges are available in almost every supermarkets including local retailers such as *Xinhuadou* and *Yonghui*. U.S. imported grocery items such as canned soup and vegetables, seasoning products; olive oils, cereals, syrups, cookies, infant formulas, dried raisins, and almonds, jams, instant-coffee are also available. Organic and natural products such as 100 percent natural juices, pancakes mix, energy bar with various tastes are becoming the new highlights on shelves. In addition, *Tesco* has plans to open one store in Fuzhou by 2010.

Xiamen retail sector is highly competitive and booming. It has several international retailers, including three *Wal-Marts*, one *Carrefour*, four *Trust-Marts* and one *Metro*. Local retailers *New Huadu* and *Minkelong* also have found niche markets. In addition to supermarkets, the city has several convenience stores and community stores such as *Beatrice*, *Tunnel 88* and *Yes*. A select group of Xiamen consumers are willing to pay a 10 – 20 percent premium to try imported products. However, typically only a limited amount of imported food products, like *Sunkist* lemons, *Red Delicious* and *Granny Smith* apples from Washington state, Thai rice and Italian olive oils, are found on shelves since retailers are more interested in offering competitively priced products to cost conscious customers. Imported alcoholic beverage products and selected snack foods are mentioned as having good potential. With rapid expansion of the retail, restaurant, hotel and tourism sectors as well as higher income levels, Xiamen market is expected to present more opportunities for U.S. agricultural products in years to come. However, the market is highly competitive so U.S. products need to differentiate themselves from competitors through pricing, unique attributes and/or strong product support. A well-defined market plan plus commitment to long-term strategy and market promotion are key.

Zhuhai is touted as a romantic coastal city in the western band of Pearl River Delta. It boasts 94 hotels and ranked third in tourism development after Guangzhou and Shenzhen. In recent years, Zhuhai has made progress in economic development due to its advantageous geographical location to Hong Kong and Macau. Retail is booming. Up to now, there are one *Jusco* and four *CR-Vanguards*. Imported food consumption is increasing. Wineshops and specially designated imported food areas attracts many expats as well as local consumers and residents from Macau. What's more, substantial investments on transportation projects will help facilitate the trade. The biggest project to be undertaken this year is the 18-mile Hong Kong-Zhuhai- Macau Bridge, which would be the world's longest sea link. Other major projects include railways (Zhuhai to Guangzhou light rail transportation for passengers commuting between Zhuhai and Guangzhou , to be completed before the *2010 Guangzhou Asian Games* held in Nov. 2010) and port facilities (four new container berths built by 2011). Upon completion, Zhuhai becomes more of a critical logistics hub for Hong Kong, Macau, Western Pearl River Delta (Zhongshan, Jiangmen and Zhanjiang) and Southwest China (Guangxi)

Nanning is considered as second tier city in Guangxi province. As Nanning's economy grows, the retail market follows suit. There are two *Wal-Mart* supercenters and three *Hualian* store, two *Nancheng Baihuo* plus two *Renrenle* in Nanning. Another international

retail giant, *Carrefour*, plans to enter Nanning by opening three stores in the newly developed commercial districts. However, this market is still in its infancy and requires indepth research and analysis as well as continued efforts to nurture the market. For many U.S. imports, Nanning is a new market full of curious customers who became affluent but lack knowledge. Local chains include *Likelong* (15 direct sales stores, 22 franchised stores, four convenience stores), *Daremen Shopping Center* (one) and *Friendship Store* (one).

Shantou has developed into a promising emerging city market with potential for U.S. food products and agricultural ingredients. It enjoys a well-developed economy and applicable consumer base. The commercial coverage reaches eastern Guangdong, southern Fujian and southern Jiangxi provinces. Urban consumers purchase international brands at supermarkets. U.S. fruits and nuts are available on shelves. International retailers *Wal-Mart* and *Lotus* (a large Thai retailer) entered Shantou years ago, and have gained tremendous popularity among the middle and upper classes. Thanks to the strong consumer purchase power, the *Wal-Mart* store in Shantou ranks the top ten in sales among all the *Wal-Mart* stores in China.

Chengdu, Chongqing and Southwest China

One in every 33 people on earth lives in Southwest China. With a population of over 200 million and a regional gross domestic product (GDP) of USD 290 billion in 2007, the area is twice the size, six times the population, and three times the GDP of Central America. The economic growth the region is experiencing is raising incomes and increasing the market for foreign products. The region is also known for its passion for food. Consumers are keen to try imported products and are willing to pay a premium for a quality product.

According to some estimates, middle-income consumers now represent almost 35 percent of urban population and at current growth rates will exceed 50 percent by 2010 and 7 percent of the total population by 2015. Economic growth in the provinces of Southwest China is some of the highest in the world, averaging between 12.0 and 15.6 percent in 2007. Growth in the regions two largest emerging city markets (ECMs) in the region, Chengdu and Chongqing, accounting for 20 percent of the region's population, reached 17 and 18 percent, respectively, in 2007.

The markets of Southwest China are less saturated with imports than developed port cities, providing several advantages to marketing products in the region. There is less foreign

competition despite burgeoning demand. In addition, marketing dollars go further because of the lower level of foreign competition in Southwest China compared to more developed markets. Finally, Sichuan food plays a leadership role in food trends. It is held in high esteem across China and influences both the national market and other regional markets.

There are three main channels for distributing products to Southwest China: local distributors which purchase their product from port cities and then sell their products to retailers; regional distribution centers, normally associated with a single retailer; and importer direct, when retailers often working with a referred importer bring products directly from the port. Regional distribution centers are responsible for purchasing and logistics for regional and national stores. Importer direct tends to be exercised by chains with less national presence, like Ito Yokado, or with highly perishable products.

Products directly purchased from port city importers and shipped directly to retailers or their central distribution centers are largely cash transactions. A significant quantity of imported products is purchased by local distributors from port city importers and then sold to the retail market. Most transactions with local distributors are carried out on a credit basis. Local distributors take on some of the retail risk by agreeing to the returns of expired or unsold products.

The higher-end hypermarkets tend to use national distribution systems, often using national purchasing managers. Metro uses this model. Retail chains with more centralized purchasing systems give local store managers less control over which imported products are on their shelves. The less centralized retailers give their local managers more control of what products are in stores, but often what is available is still determined by regional or national hubs. Carrefour and Auchan fall into this model.

Lower-end hypermarkets and supermarkets tend to use local distributors for their products. Local distributors provide more favorable terms with retailers, including paying slotting fees and selling products on credit. As a result, local distributors are reticent to offer unfamiliar foreign products with unknown market potential. This, combined with the reduced purchasing power of low end retail consumers, makes breaking into the lower-end segment of the retail sector difficult.

The majority of imported meats are purchased by retailers or their distribution centers directly from port city importers. Most imported meat is frozen. Imported fresh fruits and vegetables frequently are handled by local wholesalers. While produce is generally locally

purchased, some is directly purchased from importers. Imported processed foods are the most likely to go through local distribution channels, especially when there is no central distribution system. These local distributors will often arrange more favorable terms of agreement than central distributors in port cities, for example return of expired or unsold products. They often work on commission. In addition, local distributors tend to promote imported products through retailers to increase product sales.

Key obstacles include logistics and knowledge of how to use new-to-market products. The distance from major port cities such as Shanghai and Shenzhen is a challenge for some U.S. imports. Except for air transport, port to retail transportation time is from two to five days, and the cold chain is not always reliable.

Differentiating U.S. products' quality, safety, and value capitalizes on their reputation with consumers. The growing number of affluent consumers in Southwest China is willing to pay a premium for a superior product. In response to safety and quality concerns, the presence of "green food," the Chinese equivalent to organic, in the supermarkets has exploded. Superior quality and safety helps to differentiate U.S. products from their domestic counterparts. This is critical when competition is strong, as it is for meats, fruit, and vegetables. For this reason, it is important that the integrity of imported products be maintained throughout the distribution chain from port city to emerging city markets. Further development of the cold chain in many Emerging City Markets is essential for maintenance of refrigerated product quality. For example, a market currently exists for premium non-muscle meat poultry products, like chicken paws and wing tips.

Chengdu, the capital of Sichuan province, is the wealthiest and most advanced city in the region. Chengdu currently has the largest market for imported products.

Chongqing is growing rapidly, but incomes have not risen to the levels of Chengdu yet, so it has a smaller consumer base. Metro in Chongqing has large contracts for imported products with Yangtze riverboat tours.

Kunming and **Guiyang** are not as developed yet.

Intellectual Property Rights

We would like to encourage you to sell quality products in China and to market them exceptionally well. Of course those who intend to copy your product encourage you to do so as well. The fact that you have a quality product means that your brand has

value. Counterfeit products deprive you of that value by competing for sales with your products and harming your reputation. Counterfeit products may also be exported from China, affecting you in other markets. Protecting intellectual property is a critical part of doing business in China. Avoiding infringement requires patent, copyright, or trademark registration with the appropriate Chinese registration office. Companies must also be proactive in pursuing enforcement mechanisms available to halt infringers.

Ideally, IPR protection should begin prior to when companies or trade associations begin exploring the China market for their food or beverage goods. Interested parties should also recognize the importance of registering and protecting trademarks in both English and Chinese languages, including obtaining collective marks for U.S. collective organizations and USDA Cooperators or certification marks. Interested parties are strongly encouraged to review the U.S. Embassy’s “China IPR Toolkit” and FAS Beijing on-line reports CH7028, containing information on China’s patent, trademark and copyright legislation and enforcement and CH4078 and 7088, on plant variety protection. You can also get contact information for the FAS China IPR office at http://www.usdachina.org/en_IPR_bj.asp?functionID=110706 .

Appendix

Table 1:

Income, Spending, and Population by Province

Values converted to U.S. Dollars at Current Exchange Rate

(Data is Latest Available)

Data year:	Urban	Urban	Rural	Population
	Disposable	Consumption	Consumption	
	Income	Expenditures	Expenditures	
	2006	2005	2005	2007
	USD	USD	USD	Millions
Shanghai	\$3,336	\$2,014	\$1,064	18.6
Beijing	\$3,279	\$1,937	\$777	16.3
Zhejiang Province	\$2,918	\$1,792	\$795	50.6
Guangdong	\$2,592	\$1,727	\$542	94.5
Tianjin	\$2,263	\$1,412	\$444	11.2
Jiangsu Province	\$2,230	\$1,261	\$522	76.3

Fujian Province	\$2,209	\$1,286	\$482	35.8
Shandong	\$1,934	\$1,091	\$400	93.7
Chongqing	\$1,835	\$1,261	\$313	28.2
Liaoning Province	\$1,642	\$1,078	\$410	43
Hunan Province	\$1,630	\$1,098	\$403	63.6
Hebei Province	\$1,592	\$980	\$317	69.4
Yunnan Province	\$1,587	\$1,023	\$262	45.1
Inner Mongolia	\$1,581	\$1,013	\$358	24.1
Shanxi Province	\$1,579	\$928	\$275	33.9
Guangxi Zhuang	\$1,554	\$1,029	\$344	47.7
Anhui Province	\$1,547	\$931	\$321	61.2
Hubei Province	\$1,541	\$985	\$355	57
Henan Province	\$1,512	\$883	\$277	93.6
Jilin Province	\$1,498	\$994	\$337	27.3
Sichuan Province	\$1,480	\$1,008	\$333	81.3
Hainan Province	\$1,474	\$867	\$288	8.5
Jiangxi Province	\$1,465	\$894	\$363	43.7
Ningxia Hui	\$1,463	\$937	\$306	6.1
Shaanxi Province	\$1,454	\$974	\$277	37.5
Qinghai Province	\$1,434	\$913	\$289	5.5
Heilongjiang	\$1,422	\$904	\$372	38.2
Xinjiang Uygur	\$1,417	\$908	\$281	21
Gansu Province	\$1,402	\$955	\$266	26.2
Tibet	\$1,395	\$1,260	\$252	2.8
Guizhou Province	\$1,381	\$901	\$227	37.6
Source: China Statistical Yearbook, 2009				
Converted at 6.8374 RMB = 1 USD (interbank exchange rate from Oanda.com on Sep. 16, 2009)				

Table 2:

Selected International Retailers in Regional Markets

Number of Hypermarkets and Supermarkets by City

East China

	Shanghai	Suzhou	Nanjing	Hangzhou
Carrefour	19	6	4	2
Wal-Mart	4	1	1	3
Metro	4	4	1	1
Tesco	19	2	0	3
RT-Mart	10	9	3*	2
Auchan	4	3	3	1
Lotus	21	1	1	1

* Known as Ce Mart, a joint venture with Lianhua

North China

	Beijing	Tianjin	Qingdao	Zhengzhou	Xian
Carrefour	13	5	2	2	1
Wal-Mart	7	2	1	2	3
Sam Club	1	0	0	0	0
Metro	2	1	1	1	1
Jusco	1	0	2	0	0
RT-Mart	0	1	2	0	0
Tesco	2	5	0	0	0

South China

	Guangzhou	Shenzhen	Dongguan	Fuzhou	Xiamen
Wal-Mart	0	18	4	4	3
Trust Mart	17	4	3	5	4
Sam's Club	1	1	0	1	0
Carrefour	5	8	3	2	1
Metro	1	1	1	1	1
Tesco	2	1	4	0	1
Jusco	3	6	1	0	0

Southwest China

	Chengdu	Chongqing	Kunming
Carrefour	5	4	4
Metro	1	1	1
Ito Yokado	3	0	0
Isetan	1	0	0
Auchan	3	0	0

Source: FAS China Research

Table 3:

Top Players in Shanghai Retail Total Number of Locations, Year End 2008	
Company	Number
Lianhua	2,319
Carrefour Hypermarket	19
RT-Mart	10
Nonggongshang	2,242
Hualian	1,002
Lotus	21
Metro	4
Hualian GSM	18
Shanghai Homegain	139
Jieqiang Tobacco, Sugar & Wine	194
Auchan	4
Watson	55
Jiajiale	34
Tesco	19

Source: Shanghai Statistical Yearbook, 2009