

China Agriculture and Food, May, 2003

Alberta China Office, Beijing

General

Alberta agriculture and food product exports totalled \$297 million in 2001 of which 84% was commodities and 16% was value added product. In 2002, agriculture and food exports to China were significantly less due to a severe drought in western Canada. Based on WTO, changes in consumer eating habits and general increases in disposable income China offers opportunities for vegetable oil, beef and pork meats and branded food items.

Cereal Grains

Drought in much of western Canada significantly reduced production and subsequent export of Alberta's cereal and oilseed commodities. In 2002, Alberta exported \$14.45 million of wheat, \$10.72 million of barley, \$5.23 million canola seed, \$0.23 million peas and \$0.04 million of other cereals. 2002 export of these commodities to China decreased by \$204 million compared to the 2001 trade numbers.

China became a net wheat exporter for the first time since 1949. To encourage exports, China has deleted various fees but instituted a value added tax rebate on exported grain, reducing the cost of domestic grains by 150 RMB per tonne. High world grain prices also assisted in China's decision to export wheat.

Both urban and rural per capita consumption of wheat based products has dropped since early 90's. China's demand for wheat based products is changing with increasing demand for breads and cakes and less demand for traditional steamed bread and dumplings. Domestic production is providing wheat that can better meet needed milling properties and bakery demands. Major producing areas are Henan, Shandong and Hebei provinces. China's high quality wheat acreage reached 5.35 million hectares in 2002, yielding 21.5 million tonnes.

Barley and Malt

Alberta exported \$10.72 million of barley and \$0.317 million of malt to China in 2002 of which the barley would predominantly be for malt production.

Barley is grown predominantly in NW China, Heilongjiang, Jiangsu and Zhejiang. Primary use is in production of malt for beer. Domestic barley production meets 35 - 40% of demand. China has expanded its malting barley acreage given global barley shortage and has made substitutions with other cereals such as rice. China wants new malting barley varieties and processing techniques. China just replaced the U.S. as the world's largest beer producer; per capita consumption is 21 liters in China compared to 75 in the US. China's beer preference is light cheap lager. In 2001, China's malt output was 2.48 M tonnes (2nd in the world). The largest 100 breweries utilize 1.7 M tonnes of malt annually.

With WTO entry, the TRQ on barley has been removed and tariff rate has fallen to 3% with a 13% VAT. Malt tariff and VAT is 10% and 17%, respectively.

Canola Seed and Oil

Alberta exported only \$5.23 million canola seed and \$0.214 million crude or refined canola /mustard oil, representing a 96% drop in canola seed exports to China from 2001. The drop in exports was primarily due the drought in western Canada and to the new Chinese GMO regulations related to safety certificates and labeling.

Imported Canola oil is subject to a tariff rate quota (TRQ). The TRQ is set at 1.0186 MMT for 2003 with annual increases to 1.243 MMT by 2005, and will be eliminated in 2006. Imports within the TRQ are subject to a 9% tariff rate and 13% VAT. For oil outside the TRQ, the 2003 tariff is 26%. Expectation is that China will continue buying seed rather than canola oil due to excess domestic crushing capacity, price of crude oil and need of the meal.

China's domestic consumption for vegetable oil includes oil from soybeans (34.6%), rapeseed (31%), palm (16.1%), peanuts (16.1%), sunflower seed (1.2%) and coconut (0.8%). China is expected to require 13.7 MMT of vegetable oil in 2003, a 7% increase over 2002. In 2002, China imported 25% of its total vegetable oil needs, predominantly as seed for crushing within China.

Canola varieties (as compared to rapeseed) constitute about 60% of China's production (often mixed with rape). Land use is changing as oil and protein crops replace wheat area along Yangtzi River. One private company has indicated interest in marketing double low rapeseed oil under private brand.

China needs both vegetable oil and canola meal. Unfortunately the trade has only a minimal understanding of the difference between rape and canola with the consumer having less of an understanding. A strong consumer education program is needed. Exporters need a strong presence in China to promote their product. Changes in retail trade will be positive to developing canola oil product/brand awareness.

Genetically Modified Organism (GMO) Regulations and Labelling

The GMO product affecting Alberta is GMO canola. China has ongoing GMO variety research in a number of crops such as cotton, soybean, rice and tomatoes. Cotton and tomatoes are the only two in commercial production.

The deadline for Ministry of Agriculture issuing the permanent safety certificates have been extended to April 2004. Under the original GMO regulations, the biotech companies for each canola variety must make application for a safety certificate to MOAgriculture. All biotech companies must have the field test and safety reports to MOAgriculture by end of 2003. Until permanent certificates are issued, companies can make application for an interim certificate. Although genetically modified canola has 7 events, MOAgriculture is charging the equivalent of soybean for the safety certificate. Note there is zero tolerance to GMO contamination within shipments. All GM products (domestic or imported) are required to be labelled as such. Although MOAgriculture introduced the regulation in January 2002, it has not been enforced to date. It affects retail soybean and canola oil if MOAgriculture decides to implement. The Chinese consumer is not well educated on GMO foods and that uncertainty leads them to avoid or only buy GMO foods if price is discounted.

Chinese trading companies view the rules as not a major obstacle indicating that if price is right, China will buy. The Chinese government has given assurances that their GMO regulations will not impede trade.

Forage Seeds

China has need of forage seed for grassland rejuvenation, conservation programs to reduce environmental damages such as desertification and sand storm control, to feed expanding number of dairy and beef cattle and for city beautification. In Gansu and Ningxia, Chinese authorities are developing new alfalfa varieties for that environment.

In 2002, 95% of Canada's forage exports to China was alfalfa. Other forage seeds included fescue, Kentucky Blue Grass and clover. Canada supplied 39% of China's total forage imports (quantity basis). Although Canada exported \$11.63 million of forage seed to China in 2002, Alberta companies are recorded as only exporting \$0.113 million. Predominant reason is that Alberta companies chose to market through Saskatchewan and US affiliates.

Livestock Genetics

China has 55 million breeding beef cows of which 30% are bred by AI. Most are bred to one of the 1200 breeding bulls being collected in 40 AI centers throughout China.

Canada is one of five countries that meets the health status for export to China. Other countries are US, Australia, New Zealand and Japan. Alberta has five active export companies (beef, dairy, swine) to the China market. Export is not without its challenges. Challenges include lack of quarantine space for cattle and swine, difficulty (but still manageable) in meeting the protocol for large dairy orders, obtaining ship or plane load numbers for efficiency, and competition on price given that Australian dairy cattle can be supplied for approximately ½ the Canadian price. Canada and Alberta have a reputation of the best in quality. Canadian price quotes often include technology and training packages.

As in 2001, China is most interested in dairy genetic, particularly Holstein heifers and frozen embryos. Canada exported \$6.061 million of live cattle of which \$1.432million was from Alberta. On a world basis Canada by far exceeds other countries in value of exported semen and frozen embryos to China of which \$1.3 million was supplied by Alberta companies.

Several government departments including MOAgriculture and MOCommerce have emphasized dairy production. The major driver in the dairy business is the rapidly expanding milk consumption. Everbright, San Yuan, Yili, and Meng Niu are the top four dairy companies in China. Beef and swine genetics exports were minimal compared to dairy but all offer future potential.

Meats: Beef, Pork and Poultry

Alberta exported about \$4.69 million in beef, pork and poultry meat and offal to China in 2002 of which 69% of the value was offal. Frozen beef meat seen a 236% increase to \$788,834, fresh and frozen pork increased to \$243,908, a 296% increase and poultry meat and offal declined 31% to \$426,984 from 2001 levels. There continues a small but increasing demand for higher quality beef cuts (tenderloin, striploin and ribeye) for food service in star hotels in Beijing and Shanghai and a growing demand for imported cheaper short plate cuts. Canadian beef is recognized to be of equivalent quality to US but slightly less expensive. Australian product is much cheaper in price and of CAB (Certified Angus Beef) quality. Canadian food promotions have been successful.

In 2001, China per capita consumption of meat totals 48.5 kg of which 31.9 kg was pork, 9.6 kg was poultry, 4.2 kg was beef and 2.2 kg was mutton. Urban consumption is significantly more for all categories. The continued expansion of multinational fast food giants McDonald and KFC will ensure increasing consumption of poultry and hamburger. Beef is predominantly consumed in restaurants rather than at home. Large quantities of beef are consumed in hot pot, Korean BBQ, beef noodle and rice bowl restaurants but the beef source is domestic. Expectation of increased demand for beef, pork and poultry offal products and lower end cuts. Steakhouses exist in Shanghai and Beijing but are not popular among the Chinese.

China's views its domestic beef to have good market potential and price advantage. As such beef has been identified with several other commodities to build market image, improve quality and management. In 2002, Chinese beef was exported to Hong Kong, Russia and the Middle East. Investment is occurring in modernizing plants, increasing food safety awareness and general product quality improvements.

There were a number of meat and offal import challenges in 2002 including waiting time for sanitary certificate approvals, box labels, use of cotton gloves and new plant approvals that were negotiated by Canadian Embassy with AQSIQ (State General Administration of the People's Republic of China for Quality Supervision and Inspection and Quarantine). In 2002, Canada received approval for 30 new pork plants bringing the total number of plants approved for shipping to China to 40. Alberta has several beef plants and one pork plant approved for China.

In 2003, market challenges will include competitive pricing with Australia and US and educating distributors of the high quality of Canadian beef. Brazil has started shipping beef to China. Note that the Canada Beef Export Federation has offices in Shanghai and Hong Kong.

Value Added Food Sector

Alberta exported to China about \$28 million of value added items, excludes meats in 2002. The largest was hides at \$26.5 million. If meats and hides are excluded from the calculation, then there was a 45% increase in value added processed food from Alberta exported to China. Alberta companies exported margarine, frozen juices, frozen vegetables, flour, potato granules, water, whey and some branded specialty items to China.

China's retail food service industry is changing. Carrefour and Wal-Mart are pushing Chinese companies to change. Their influence combined with Chinese consumer's interest for new products will increase the diversity and quality of food products. Supermarkets and convenience stores are increasingly stocking time saving foods that are ready to heat and eat, ie. frozen precooked foods, convenience store foods, snacks. Beijing, Shanghai and Guangzhou are the preferred target markets for most imported new food items.

The Alberta China Office has been active in meetings with importers and distributors at the food service level, food promotion at star hotels, and listing of food suppliers to Beijing. We have also been in contact with Alberta suppliers to initiate business introductions and provide information and assess their interest in China. One of the most visible Alberta value added food item in Shanghai and Beijing food stores is "Canola Harvest" margarine.

Future Opportunities

Increasing disposable income and a general love of sports sees wealthy families interested in renting or owning horses at local stables. Potential exists for the recreational horse industry including pleasure, equestrian and racing to develop relatively fast given Beijing 2008 Olympics. China could see changes to gambling rules whereby the race horse industry will become established. At this time a major limitation for Canada is a lack of a horse protocol between China and Canada (being considered). Alberta companies can participate at several levels including genetics (if protocol is established), horse tack, veterinary care, feed, education, and consulting. Already there are requests for rodeo in Beijing. Of particular interest for genetics would be the Alberta Quarter horse.

China is paying much attention to food safety. Presently about 25% of China's food is processed. For Alberta companies, there would be opportunities for consulting, especially in the dairy and

meat business for food safety, food processing expertise. Technology that enhances production efficiency, food safety, processing technology are all of interest in China.

38% of China's population is less than 26 years of age. Being the only child, growing up in expanding prosperity, having parents who value you being educated, and having been exposed to international affairs, the young consumers in China are open to new experiences, including world food experiences. Integrated western products into traditional Chinese cuisine will enhance acceptance.

Investment in Alberta

Chinese companies are becoming wealthier and want increasing access to North American meat markets. Presently, SPS issues restrict export of meat to North America, creating the opportunities for Chinese genetic, meat and produce companies to invest in Alberta. The Alberta Office will continue to pursue educating select Chinese companies in the Alberta Advantage.

Alberta Companies involved in China CIDA Projects

Alberta companies are participating in CIDA INC projects in China in the following areas: pumpkin and sunflower export and development; alfalfa production; tree seedling and horticulture nursery development, consulting related to agriculture village management and beef production.

WTO and Agriculture

The joining of WTO resulted in the immediate reduction of some tariffs with a structure for further tariff reductions to 2004 or 2006 depending on the commodity. To date China has basically complied to its WTO commitments. But China has also introduced non tariff barriers to slow market opening (ie payment of bills, custom clearance, GMO labeling). In the long term, will see improved transparency but in the short term some business confusion. China expects continued increases in foreign direct investment.

Please direct questions to:

Rob Hand
Agriculture Manager,
Tel: (86-10) 6532-3536 ext. 3612
Fax: (86-10) 6532-1304
Email: rob.hand@dfait-maeci.gc.ca

Jenny Luo
Agriculture Commercial Officer,
Tel: (86-10) 6532-3536 ext. 3613
Fax: (86-10) 6532-1304
Email: yajie.luo@dfait-maeci.gc.ca

Alberta China Office
Government of Alberta, Canadian Embassy
19 Dongzhimenwai Dajie
Chaoyang District, Beijing 100600
People's Republic of China