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Who's feeding China's offspring? Baby food market indicates strong

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Summary: Baby food products are the fastest growing product category in China's supermarket retail sector. As China's economy expands, stronger purchasing power and increased living standards are enabling greater consumer demand for high quality baby food including imports. The country's emerging urban middle-class consumers are willing to pay a premium for high quality imported baby food and nutrient products and are especially leery of domestically produced baby food products even when these have foreign brands. With a post-2008 melamine tainted milk scandal still lingering in the minds of distrustful middle class consumers, global infant product manufacturers are pushing their way to seize market share or find a niche in this promising market. However these products are not limited to infant formula as local baby food producers are anticipating 90-percent growth in the industry by 2014. On August 14, 2012, China's Ministry of Health convened a press release and provided official response to the recently heated topic of "colostrums milk powder prohibition".

General Information:

Starting with the Goodness

Parents want the best for their children. They attach importance to feeding their babies (one per household) quality ingredients containing sufficient nutritional components. Babies roughly between 0-years are considered infants when they need to be with specifically made infant formula and other food. Infants can only consume soft and watery-food. Other than breast milk, infant formula is the major food to begin with, followed by other supplements such as dried baby food like cereals, ready-to-eat baby food and snacks, as well as nutritional beverages. Breastfeeding for babies beyond six months is usual among Chinese women. Homemade baby food is also traditionally common in Chinese families where infants are fed rations of rice porridge with mashed fruit and vegetables. As the market witnesses commercial baby food flying off of retail stores shelves and with dramatic prices difference and gaps based entirely on brand-recognition, these items are being promoted in convenience stores and community stores in every first, second and third tier city in China. More and more Chinese parents tend to purchase a variety of imported baby food, particularly in urban households with rising per capita disposable incomes. Generally speaking, baby formula and instant baby paste (whey/rice cereal) are the two most widely consumed baby food items in China.



Picture source from Reuters

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3
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Figures Speak Louder than Words

China is the second largest baby food and infant formula market in the world. According to National Bureau of Statistics of China, the annual average birth rates in China (in the last four years and forecasting until 2017) reach around 15 million~17 million. Typically, the industry refers to “baby food” as infant food or food for children under 3 years old. If we take the average birth rate of 160 million and multiply it by 3 (the first three years when infants consume baby food), the annual baby food targeted per individual baby will be around 50 million. The annual average baby food per household expenditure is around \$800, which means China is a \$40 billion market. Another market research by a recognized investment consulting firm also indicates that disposable expenses spent on infants in 1st and 2nd tier cities run around \$950-\$2,800 per year.

Recent statistics conducted by China Baby Products Industry Research Center show that there has been a steady growth of 15 percent per annum in China’s baby products market over the past ten years. Moreover, data from Euromonitor International demonstrates that out of the \$41 billion global baby food market, China accounts for 23 percent of the total.

A market research report on “China Baby Food and Infant Formula Outlook in 2016” illustrates that China’s baby food and infant formula milk market retail sales reached \$3.281 million in 2007, while in 2009, the segment grew by 21 percent. Infant formula has marked a growth in sales of 14 percent in 2011 relative to the increase of 14 percent and 16 percent in 2010 and 2009, respectively.

Fierce competition in the baby food market

Global baby food manufacturers are striving to consolidate and seize greater market share worldwide. Many are branding their products with their own standards which are backed-up by a particular's country's pediatric associations. According to market research conducted by a popular Chinese food and beverage website (http://news.40777.cn/info_71310.html), the top ten international infant formula manufacturers (in no particular order) that are dominating the China market include:

- Mead Johnson (U.S.)
- Dumex (Europe)
- Nestle (Switzerland)
- Wyeth (U.S.)
- Abbott (U.S.)
- Meiji (Japan)
- Anmum (New Zealand)
- Ausnutria (Australia)
- Morinaga (Japan)
- Friso (Holland/Germany)

Some large producers, such as U.S. infant formula group Mead Johnson, the top player with the largest market share in China remains confident with improved earnings in 2012 amidst a slight decline in the sector's (specific to infant formula) overall growth rate in 2011. Other manufacturers like Nestle, who recently (in 2011) acquired Pfizer Inc.'s baby food unit, now aim to regain momentum in China's baby food market after its untimely departure from the China market back in 2005.

Post has conducted market research at four high end supermarkets chains (Ole, Taste, Jusco and Parknshop) in Guangzhou with individual sector on baby food. Baby food areas in these four retail stores are teeming with customers and promoters. One supermarket even has at least ten in-store promoters recommending infant formulas to consumers and a baby playing pin area so that parents can listen to the promoters as they are charmed into purchasing a particular brand of baby food. Dominating baby food brands are either products imported with original package, or foreign brands with raw material imported but packaged in China. The target buyers of these brands are mostly middle class consumers both male and female according to in-store staff. According to feedback from supermarket retailers, for baby milk powders, foreign brand names of milk powder manufactured in China such as Mead Johnson, Abbot and Wyeth, are widely accepted because of a perceived reliability by consumers in quality and their affordability in price. The retail price for a tin of milk powder 800gram falls largely between \$27~\$40 (RMB170~RMB250).

On the other hand, directly imported baby milk powder is becoming increasingly popular among Chinese consumers. Most of these products come from Germany, Holland, Switzerland, Australia, New



A baby food sector in one of Guangzhou's famous retail store

Zealand and Japan. However, of all the retail stores Post visited, none of the directly imported baby milk powder from the United States. Almost every single overseas manufactured milk powder will have the wording of “imported with original package” (原装进口) on the commercial package to catch consumers’ attention. Retail prices for these products range from \$46~\$56 (RMB290~RMB350), which are comparably higher yet demand is strong.

Although 90 percent of the infant milk powders are cow milk, some of the competitors from Holland and New Zealand have recently began to market **goat milk formula**. Studies have shown that mineral substance and protein proportion contained in goat milk is closer to human milk than bovine milk, which is considered healthier, more nourishing and easier for babies to digest.

Traceability is a value added advantage which reassures parents when they purchase baby formula. One Dutch company established an online traceability system that allows consumers to trace back to the cultivated farmland, raw milk collection, as well as important links of production and transportation in order to improve the customers’ confidence and loyalty.

With regard to other supplemented baby food, the most widely available brands are Heinz, Gerber (under Nestle) and Biostime. These three main competitors all have production bases in China. According to retail stores’ baby food promoters, Heinz is the considered a reliable brand by most consumers with the widest variety of baby food in the market. Heinz also established an Institute of Nutrient Science in China which is dedicated to improve nutritional structure. And, the company has already shaped solid consumer loyalty in the market. There is no directly imported baby food available in China. Only one German organic baby food brand can be found in local large supermarkets.

China’s Newly-Published “Colostrums Milk Powder Prohibition”

On August 14, 2012, China’s Ministry of Health convened a press release and provided official response to the recently heated topic of “colostrums milk powder prohibition”. Basically no colostrums powder is allowed in three product categories inclusive of:

1. Infant (0~12 months) formula(*definition from the People’s Republic of China National Standard(Guobiao) GB10765-2010*)
2. Older infants (6~12 months) and young children(12~36 months) formula (*definition from the People’s Republic of China National Standard(Guobiao) GB10767-2010*)
3. Infant formula with special medical purpose.

Representatives from China’s Ministry of Health claim that colostrums milk powder with low production quantity is difficult to collect and the quality is unstable making it an unsuitable ingredient for processed baby formula. This stipulation will become effective on September 1, 2012. Beforehand, all legally produced or imported baby formulas with colostrums milk powder within expiry date are still allowed for sale.

Organic Baby Food

Organic food is also a fast growing sector in China. An increasing portion of affluent parents, with higher baby health consciousness, feel the need to purchase organic baby food even though the cost may

be double in price when compared with conventional baby food products. Many reports on the internet discuss the development of allergies which are brought about the use of chemicals possibly contained in conventional baby food.

Organic baby formula and supplementary foods are emerging in China's 1st tier cities. Wording such as "Organic", "Imported with Original Package" "Pure and Safe" usually appear on the commercial packaging; however there is no standard or regulation on the use of these subjective marketing terms. It is also mandatory for all foreign organic products to receive the China Organic seal approval before entering into the retail sales channel. Thus, all of the organic baby food will have the organic product seal printed on the packaging as well. Most of the organic baby food emphasizes the idea of food safety, better nutrients and environmental-friendliness. Take baby formula for instance, manufacturers claim that throughout the entire production process, pesticides or fertilizers are not utilized for forage grass plantation, no genetically modified bovine feed ingredients were allowed, and no growth hormones were injected in the animal to raise its milk output. Also, edible food additives are strictly forbidden to be added to the production of all types of baby food. Although the retail price for a tin of 800 gram organic baby formula is much higher (around \$73/RMB 460), an increasing number of affluent parents are still willing to pay a premium for the "organic" label.

According to research conducted by Innovative Research and Products (iRAP), Inc., the global market for organic infant food will increase to \$2.26 billion by 2012 compared with \$760 million in 2007. In the long term, Southeast Asia countries now the largest producers and exporters of snack food to China will likely emerge as producers for organic baby products. However, these countries will need to import their raw materials for third countries such as the United States, Switzerland, Australia and New Zealand.

What influences Nursing Mothers' Choice for Baby Food?

According to the United Nations' World Health Organization and UNICEF, parents are recommended to wait until a child is six months of age to switch from breast milk to powdered milk. Consequently quality baby milk powder is most crucial during the initial substitution. Usually, there are three different types of milk powders, inclusive of infant formula for 0~12 months of age, "follow-on" formula for 6~18 months of age and "growing up" formula for 1~3 years age. Many Chinese mothers believe in the philosophy of "breast is best". Breast milk is said to be the best food for new-born babies which consists of all the essential nutrients and elements with the right proportions required for infants' growth and overall development. When mothers choose infant milk powder, they tend to select formulas that are closest to human milk. Many of the well-received brands packages will highlight that their formulas are proximal to breast milk with similar protein proportions to strengthen infants' immunity, 1,3-dioleoyl-2-palmitoyl-glycerol (OPO) to protect babies from enteric infection and allergy, as well as long chain fatty acids including DHA and ARA to improve brain and retina development.

Chinese also believe that excessive "heat" (food that leads to bloating or excessive fluid retention) inside the body generated by the food consumed may trigger disease. Nursing mothers are more inclined to pick formulas without palmitic acid, which has been considered a primary reason to create "heat" (in this case inflammation) to the infant's body, and influence babies' nutritional absorptive and digestive functions. Although medical experts have a negative attitude toward this argument, most commercial brands tend to label products "containing non palmitic acid" as a marketing tool when promoting their infant formula products.

With the exception of milk powders, a variety of baby food is swarming into the market. While choosing ready-to-eat baby food such as whey cereals, colostrums milk powder, vegetable and fruit-based purees, mashed noodles, teething rusks, mothers will select products without edible additives like flavoring essence, sugar cane, maltodextrin and thickeners. It is also stipulated by Ministry of health of China in the Notice 21 issued in 2008 that no edible flavoring essence should be added to any kind of baby food for infants between 0~6 months.

Nursing mothers will also communicate with each other through internet when deciding which brand of baby formulas to purchase, and when to start feeding infants for supplementary food. There are several well-known websites in China such as Mama.com (<http://www.mamacn.com/>) and Pacific Baby (<http://www.pcbaby.com.cn/>) with countless information for parents to share their experience and knowledge. From time to time, these popular parental guidance websites will launch baby food item appraisals through comparisons to offer more “unbiased” reference points to Chinese parents.

Consumer Trends

Although directly imported baby food and infant formula tend to have a higher price, Chinese parents have been shifting to international brands with demand towards higher quality and safer products. On another hand, many parents prefer to purchase healthier formulations instead of the ready-to-eat baby food added vitamins and calcium, for instance. Public concern over domestic powdered milk formula still prevails two years after the melamine-tainted milk

scandal, which has indirectly enabled sales growth and opportunities for more and more foreign brands of baby food to enter the market and establish credibility over domestic brands.



with

A mainland Chinese consumer purchased large case of infant milk powder from a local Hong Kong Retail Store

Chinese parents living in South China, particularly those from the Pearl River Delta enjoying geographic proximity to Hong Kong are streaming across the border for high quality infant formula, especially when the rise in China's currency has also made Hong Kong products relatively less expensive than those sold in the Mainland market. Many of these baby products carried over from Hong Kong are sold in Taobao, a Chinese website for online shopping similar to eBay and Amazon. Some overseas Chinese living abroad even purchase baby food on Mainland internet shoppers' behalf and deliver the products directly to China through express mail. Thousands if not close to a million consumers from Mainland China routinely snatch milk powder from Hong Kong and sell to Mainland parents either through internet retailing or other channels. The demand is so great that Hong Kong retailers have to limit purchases to four per costumer.

Future Opportunities

Rising consumer power and growing awareness on food safety will continue to fuel the baby food market demand in China. While there have already been a number of directly imported baby food items from Europe, Australia and New Zealand, it is time for other U.S. brands to seize this golden

opportunity and access the China market-- particularly when organic baby formula and goat milk formula will remain as a niche market and competition is yet to be challenged by domestic producers.