THE CHINESE WINE MARKET

OPPORTUNITIES AND THREATS

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Since 1990, China has been experiencing tremendous economic growth. The worries of 2001 were put aside in 2002: growth reached 7.9% during the first three quarters. There are two possible explanations for this economic dynamism : China's entry into the World Trade Organization (foreign investments jumped by 22.6% compared with the same period in 2001), and, in November, the signing of a free trade agreement in Phnom Penh with the 10 members of the South East Asian Countries Association, giving birth to the world's largest free trade zone.

Changes have been so dramatic during the last couple of years that even the Communist government had to acknowledge the economic development by accepting the involvement of the business community in the upper part of the state apparatus. The boom in the private sector can be illustrated by some simple figures: the number of private companies has increased by 35% per year since 1990; the private sector represents today 25% of industrial production, a third of the GNP (excluding Agriculture) and 11% of employment (according to official figures that are probably underestimated).

This dynamic environment coupled with the increase in the population's wealth and education should benefit the wine sector. In addition, the wine sector should also benefit from a drop in customs duties on wine imports from the current 60% to 14% in 2005 (due to the WTO entry), and the economic boost provided by the 2008 Olympic Games and the Universal Exposition in Shanghai in 2010.

Table 1 : China at a glance

	Population (millions)	GNP per capita. ($)	Inflation (%)	Unemployment (%)
China	1 272 (26% less than 15 years old)	890	-0.8%	3% (official) – 8-10% (unofficial)

Source : OCDE 2002

I - Wine production in China

Total area under vine in China is estimated at around 210 000 ha (from private sources, as official statistics are not reliable), with about 60 to 70 000 ha planted with western varieties.

Table 2 : Chinese vineyard 1986-2001

	ha	Evolution %
86-90	143 000	n.c
91-95	148 000	3.50%
1996	165 000	11.49%
1997	172 000	4.24%
1998	194 000	12.79%
1999	200 000	3.09%
2000	206 000	3.00%
2001	210 000	1.90%

Source : Vertumne - OIV

Fewer than 240 wineries were officially registered in 1996. Now there are more than 350, mostly smallholders. At the beginning of the 1980's, there was a boom in foreign investment in the Chinese vineyard, mainly by large French companies : Castel, Pernod Ricard, Remy Cointreau, Groupe Taillan, and William Pitters. Unfortunately, due to the difficulties of the current economic situation and the lack of proper long term financial assistance, most of these companies have withdrawn a large part of their involvement in China. They do, however, keep an eye on the market.

In 2001, 250,000 tons of grapes were harvested. Even if most of these grapes were used to make wine, it is very difficult to estimate Chinese wine production. The term "*putao jiu*" is used to identify wine made from grapes, but it also includes alcoholic drinks made with more than 50% wine must: rice wine composed of more than 50% grape must be included in the "putao jiu" category.

According to official statistics for 2002, 4 million hl were produced (45-50% pure grape wine), compared with 3.8 million hl in 2001.

Table 3 : Wine production in China 1986-2002

	hl	Evolution %
86-90	2 734 000	n.c
91-95	3 120 000	14.12%
1996	3 000 000	-3.85%
1997	3 200 000	6.67%
1998	3 550 000	10.94%
1999	3 800 000	7.04%
2000	3 900 000	2.63%
2001	3 900 000	0%
2002	4 000 000	2.56%

Sources : Vertumne International

II. Wine Consumption in China

Precise figures of wine consumption in China are difficult to obtain: firstly, what constitutes "wine" is not clearly defined, and secondly, counterfeited products enter the market from Hong Kong and other eastern countries. In addition, since 1996 the Chinese government has been trying to slow down hard liquor consumption and encourage wine consumption, this through several actions favouring domestic wine production and the bottling of imported bulk wines in China. However, wine still accounts for a small percentage of China's alcoholic drinks market compared to beer, white spirits (Chinese liquor), and yellow rice wine. Consumption can be estimated at around 6 million hl.

Table 4 : Wine market in China 1994 – 2005

	M hl	**Evolution %**
1994	3.46	n.c
1997	4.74	36.99%
1998	5.00	5.49%
1999	5.30	6.00%
2000	5.60	5.66%
2002 (e)	6.00	7.14%

Source: Chinese Customs + Ministry of Finance

Wines from China's western regions and foreign countries are the two major new forces on the market today. Yet, despite competition between domestic and foreign wines, only three Chinese brands (Changyu, Dynasty and Great Wall) have market coverage nationwide (see Table 4). These three brands however account for more than half of China's wine market share.

Table 5. Leading Brands in China's Wine Market

Brand Name	Company Name	Location	Year Founded
Changyu	Yantai Changyu Group Co., Ltd.	Shandong Province	1914
Dynasty	Sino-French Joint Venture Dynasty Winery Ltd.	Tianjin City	1980
Great Wall	China Great Wall Wine Co., Ltd.	Hebei Province	1985

Source: Channel Consulting Ltd

China's wine consumption has been continuously increasing since the late 1990's. The per capita consumption of wines rose from 0.19 litres in 1997 to 0.29 litres in 2002, representing a 53% increase (see Table 5). Nevertheless, compared to France (59 litres), UK (22 litres), USA (12 litres) or even Japan (3 litres), China's per capita grape-wine consumption is still far behind.

Table 6. Per Capita Consumption of Wine in China 1997 - 2002

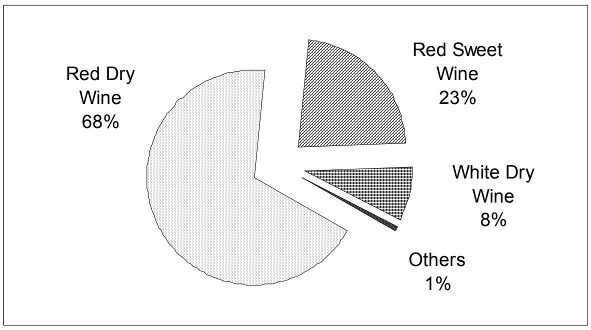
	1997	1998	1999	2000	2001	2002
Per Capita Consumption (litres)	0.19	0.22	0.24	0.27	0.28	0.29

Source: Channel Consulting Ltd.

Domestic wine consumption is dominated (85% in volume) by domestically produced products, but has significantly evolved over the last few years moving from a 5-95 white/red consumption ratio to 80-20 in favour of red today.

The preferred type of wine varies from region to region. For example, sweet red wine is more popular in the northern part of the country than in the south. Nationally, dry red wine is still the most preferred type of wine by Chinese consumers, and sweet red wine holds the second position. (see Chart 1)

Chart 1. Consumer's Preference of Wine Type



Source: Channel Consulting Ltd - Peking

Wine sales in China have also dramatically changed over the last few years, mostly due to the influence of western supermarket chains and the strong development of hard discount stores. It can be estimated that around 65% of wine sold in China is through the supermarket channel, compared to less than 1% through specialised retail stores.

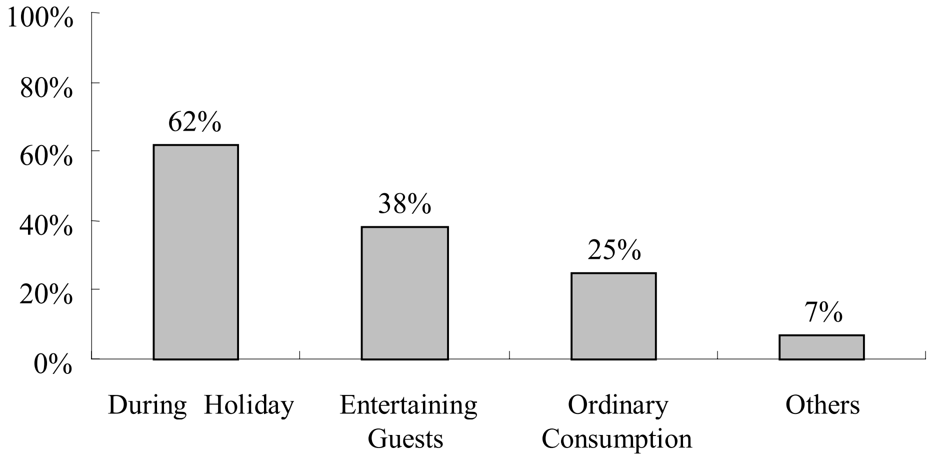
Table 7 Place of purchase of wine in China in 2002

	2002	**Trend**
Supermarket chains	65.00%	Strong development
Hotels, restaurants and clubs	25.00%	increasing
Bar	9.00%	increasing
Specialised stores	1.00%	stable

Source: Ministry of Finance - Peking

Wine consumption in China is also influenced by holidays, during which consumers tend to drink more than the rest of the year. (see Chart 2).

Chart 2. Chinese Consumer's Conditions of Wine Consumption



Note: Multiple answers, the total exceeds 100%.

Source: Channel Consulting Ltd.

Generally speaking, the higher the consumer's income and education, the more likely he/she is to drink wine. In addition, the number of male wine consumers is 19% higher than female consumers, and the 25 to 44 age group is significantly larger than others, accounting for 60.5% of total consumers. It's clear that young, middle-aged males with a high income and education are the major wine consumers in China.

III. Foreign Wine in China

Bulk wines represent by far the largest quantity of Chinese wine imports, with Chile becoming the main supplier in 2001, taking advantage of the sharp drop in Spanish imports. It should be noted that a big part of the imported bulk wine is blended with many Chinese brands and is therefore not sold as imported wine.

Table 8 : Bulk wine Imports in China (1999 to 2001)

	1999		2000		2001	
	Litre	USD	Litre	USD	Litre	USD
Bulk wine	**Volume**	**Value**	**Volume**	**Value**	**Volume**	**Value**
France	4 616 445	3 487 360	3 686 989	2 628 499	2 889 217	1 744 333
Spain	28 404 969	17 286 540	20 692 682	13 193 407	7 704 606	4 768 593
Italy	5 401 187	4 140 961	5 312 436	3 627 953	4 234 270	2 848 599
Chile	748 688	804 419	1 513 780	1 491 413	9 910 987	5 972 131
USA	705 281	894 299	908 303	1 394 364	950 010	1 182 149
Australia	182 657	171 202	120 792	63 644	1 603	7 898
Total	**40 444 173**	**27 044 675**	**32 343 944**	**22 544 000**	**26 538 429**	**17 133 593**

Of both still and sparkling bottled wines, France is the leading supplier with more than 40% market share. However, the current image of French wines in China has been heavily disturbed by recent scandal. In 1999, the rumour that cow blood had been used in previous years (and forbidden since then) during wine production as a fining agent came as a shock to Chinese consumers. Some of them made a link between French, and foreign wines in general, and the mad cow disease. In addition, the news that potentially fake Bordeaux wines were being sold came out in February 2002, confusing this immature market and greatly weakening the image of foreign wines overall.

Table 9 : Still wine Imports in China (1999 to 2001)

	1999		2000		2001	
	Litre	USD	Litre	USD	Litre	USD
Still wine < 2L	**Volume**	**Value**	**Volume**	**Value**	**Volume**	**Value**
France	1 275 412	3 005 687	651 015	1 765 891	990 921	2 422 437
Italy	475 359	882 082	328 628	734 109	186 955	426 693
Spain	289 065	419 856	59 718	127 979	91 017	245 476
USA	426 783	860 417	292 795	496 286	371 103	566 921
Australia	335 499	855 275	266 019	660 374	428 519	800 273
Chile	16 461	42 607	182 912	493 188	35 921	78 355
Total	**3 103 291**	**6 695 561**	**1 992 513**	**4 906 000**	**2 324 817**	**4 976 985**

Table 10 : Sparkling wine Imports in China (1999 to 2001)

	1999		2000		2001	
	Litre	USD	Litre	USD	Litre	USD
Sparkling wine < 2L	**Volume**	**Value**	**Volume**	**Value**	**Volume**	**Value**
France	34 357	119 000	93 762	447 440	143 044	1 143 426
Italy	17 994	30 000	97 631	79 298	45 615	82 206
Spain	0	0	13	55	4 655	12 545
South Africa	0	0	450	1 180	1 477	3 907
Germany	24 377	34 000	24 115	84 498	25 244	39 555
Australia	21 314	40 000	7 802	16 092	10 752	25 421
USA	1 831	3 000	2 087	14 000	76 812	133 995
Total	**110 521**	**246 000**	**234 911**	**669 000**	**356 302**	**1 483 981**

Source: Chinese Customs

Sparkling wine imports are relatively small compared to bulk or still wines and are not significant compared to the quantity of locally produced Chinese sparkling wines, which represent 99% of the market (mostly cheap wines bottled in 1.5 litre bottles).

When foreign wines first entered the Chinese market, they enjoyed a "noble" image due to their unaffordable price for most of Chinese consumers. Nowadays, the "status identification" fever is over and Chinese consumer behaviour is becoming more reasonable and personal. Foreign wines are now facing two major obstacles on China's market: brand unfamiliarity and price uncompetitiveness.

Although imported wines currently maintain the dominant position in the premium wine segment (particularly in top hotels and restaurants), foreign wines are not yet popular in China. While Chinese wine consumers are very familiar with domestic brands such as Changyu, Dynasty and Great Wall, very few know anything about foreign wines. This makes it difficult for Chinese consumers to distinguish different foreign wines and choose the right one for their purchase.

On China's market, most foreign wines are sold over RMB[1] 40 (4.8 US$) per bottle, while the typical Chinese consumer usually buys wines that are priced around or under RMB 30 (3.6 US$) per bottle. Because of the high price sensitivity of Chinese consumers, this price gap makes a big difference. It also appears that Chinese consumers are starting to realise that domestic Chinese wines in the RMB 40-55 range are often of better quality than the imported foreign wines sold at RMB 75-95.

[1] RMB = Renminbi – 8.27 RMB=1US$

Although foreign wines are on the shelves of supermarkets and specialty shops in many cities, imported wines are still mainly sold in hotels, restaurants and nightclubs.

When it entered the WTO, the Chinese government promised to decrease the tax on imported bottled wines each year. By 1 January 2004, this figure should finally be cut to 14 percent (see Table 3). Although a lower import tax cannot solve every problem, it will certainly improve the situation of foreign wines in China by helping to reduce the price gap between foreign wines and domestic wines. The price advantage of domestic wine won't be as significant as before.

Table 11. China's Import Tax Rates on Wine[2]

	2001	2002	2003	2004
Bottled wines (less than 2 litres)	44.6%	34.4%	24.2%	14%
Bulk wines	47%	38%	29%	20%

Source: Channel Consulting Ltd.

IV. Conclusion

China is a relatively young market and difficult to evaluate. Many observers agree that China is over-stocked with wine (some reckon about 3 to 5 years of stock). Whatever the real size of the Chinese market, a long term consistent potential can be foreseen. In fact, according to the US Wine Institute, even though only 8.3% of the population can afford to drink wine today, this figure still represents 100 million people.

The Chinese market also deserves interest because of a change in consumer attitude: more women are drinking wine than before. Recent issues of popular magazines and newspapers have extolled the health benefits of drinking wine.

The prospective growth of the market could also be boosted by the potential of the planned reduction in import taxes due to China's joining the WTO as well as by growing market opportunities in cities like Hangzhou, Suzhou, Nanjing, Tianjin, and Dalian, situated in the more developed eastern part of China.

The Chinese market will however live up to expectations only if investment is made in consumer education: the average Chinese consumer knows very little, if anything, about wine, so it's no wonder that 90% of the Chinese market is dominated by low quality wines. Generally, in wine-producing countries consumer wine education campaigns are spearheaded by local producers. Lets hope that this will be the case for China.

[2] In addition to import taxes, a value added tax of 17% plus a consumption tax of 10% is added.