



**INTERNATIONAL
COFFEE
ORGANIZATION**

ICC 115-7

10 August 2015
Original: English

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International Coffee Council
115th Session
28 September – 2 October 2015
Milan, Italy

Coffee in China

Background

In accordance with Article 34 of the International Coffee Agreement 2007, the International Coffee Organization is required to provide Members with studies and reports on relevant aspects of the coffee sector. This document contains a report on coffee in China.

Action

The Council is requested to take note of this document.

COFFEE IN CHINA

I. INTRODUCTION

1. In recent years, both the production and consumption of coffee in China have been growing at double-digit rates, and show few signs of slowing. It is estimated that China now produces more coffee than Kenya and Tanzania combined, and consumes more than Australia. As the economy of China continues to grow, the pool of consumers with disposable income expands and demand for coffee rises accordingly. The presence of coffee shops is no longer a novelty, but rather an essential feature of the urban landscape. Although still predominantly a tea-drinking nation, China is rapidly developing a taste for coffee, which could have significant implications for the world market¹.

II. COFFEE CONSUMPTION IN CHINA

(a) Overview

2. Estimates of coffee consumption in China are somewhat hampered by the lack of reliable statistics. However, it is possible to derive an estimate based on production, export and import figures, which are more readily available. The results of this analysis suggest that coffee consumption in China came to around 1.9 million bags in 2013/14, and has been growing at some 16% per annum over the last ten years². This level of consumption would make China the 17th largest coffee consumer in the world. With a population of 1.4 billion people, however, per capita consumption comes to just 83 grams, or 5 to 6 cups per year, although again this is growing. Furthermore, per capita consumption is believed to be significantly higher in urban areas, and has been estimated at 2 kilograms in Hong Kong, compared to 4.9kg in the European Union or 4.4kg in the USA.

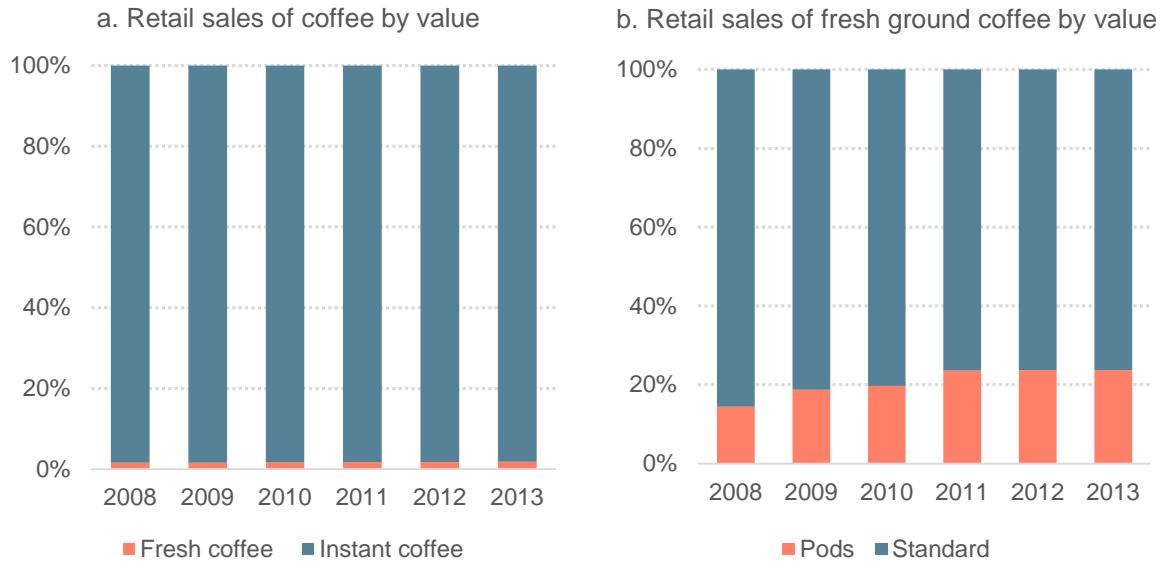
(b) Market structure

3. According to market research firm *Euromonitor*, the Chinese coffee market is predominantly composed of instant coffee. Indeed, instant coffee makes up around 99% of retail sales by volume and 98% by value, although fresh roasted coffee is growing at a faster rate. The most popular types of instant coffee are the 3-in-1 products which contain coffee, sugar and whitener, as well as potential flavourings. Nevertheless, the rising popularity of coffee shops and coffee culture in general is promoting growth in fresh roast and ground coffee. Furthermore, on-trade sales are increasing faster than retail sales, with the number of café outlets in China estimated at 13,834 by the end of 2013. As disposable incomes rise, consumers tend to 'trade up' to a more premium product. The most dynamic growth is found in retail sales of coffee pods, although in absolute terms they remain a niche category.

¹ This study refers to 'China' to include the Special Administrative Regions of Hong Kong and Macao. Unless otherwise stated, figures are given on a crop year basis, i.e. October – September.

² Full details of this methodology can be found in the Annex.

Figure 1: Market composition of retail sales by value



Source: Euromonitor International

4. Despite this growth, China remains overwhelmingly a tea-drinking nation, with retail sales of tea outweighing coffee by almost ten to one. However, in the foodservice sector, coffee commands a stronger market share, up to 44% in calendar year 2013. The foodservice sector is still small by comparison, but reflects the growing preference for coffee demand in the social or out-of-home sector. Furthermore, the rapid development of commercial chains and coffee shops shows the potential for further growth.

Figure 2: Market shares of tea and coffee in the retail and foodservice sectors



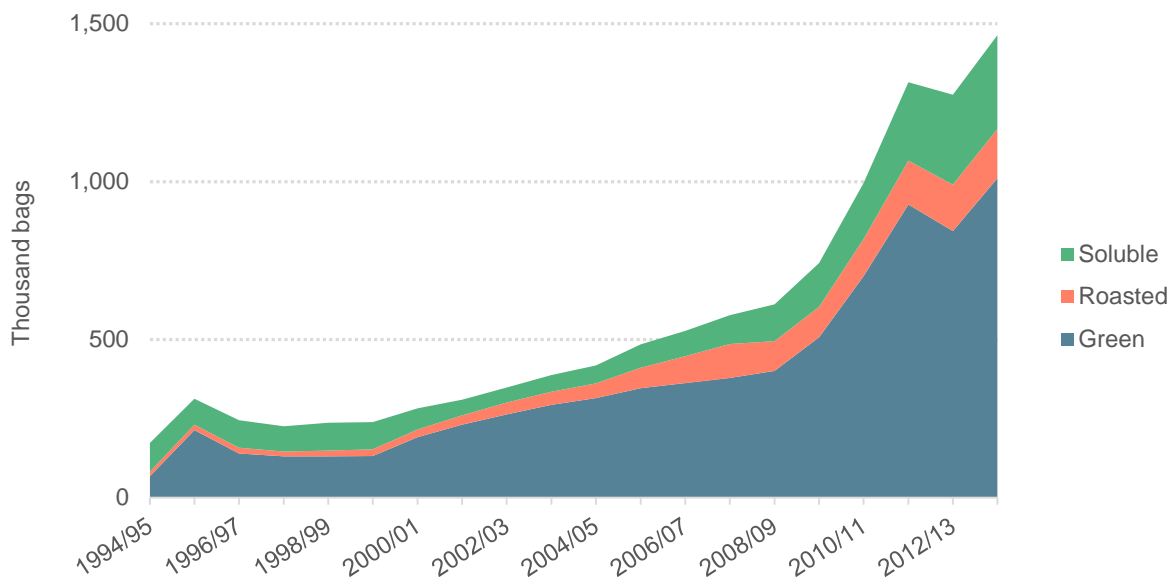
Source: Euromonitor International

(c) Imports

5. Total coffee imports by China in 2013/14 came to 1.4 million bags, compared to 418,000 in 2004/05. There has been a substantial increase in imports over time, growing at an average annual rate of 15% over the last ten years.

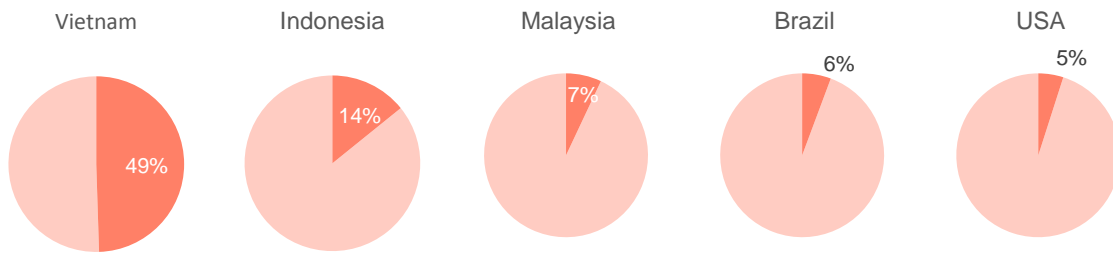
6. Coffee imports are mostly in green, unprocessed form, accounting for an average of 69% over the last five years. In 1994/95, a much greater proportion of imports were of soluble coffee; the resulting decrease could potentially be attributed to the development of a local processing industry following investment from Nestlé to help meet national demand. Over the last five years, however, soluble imports have been increasing rapidly, presumably as national demand increases faster than domestic processing capacity.

Figure 3: Coffee imports by China by form of coffee



7. In terms of origins, the biggest supplier of coffee to China is Vietnam, which accounted for almost half of all imports from 2009/10 to 2013/14. Over 80% of imports come from just five countries (including re-exports from the USA), as shown in figure 4 below. Based on these origins, and information from external sources, it seems likely that the significant majority of coffee imported into China is Robusta, which reflects the preference for soluble coffee. However, it is worth noting that imports from Colombia and Central America have been increasing significantly in recent years, at over 25% per annum since 2009/10, and now make up around 5% of the total.

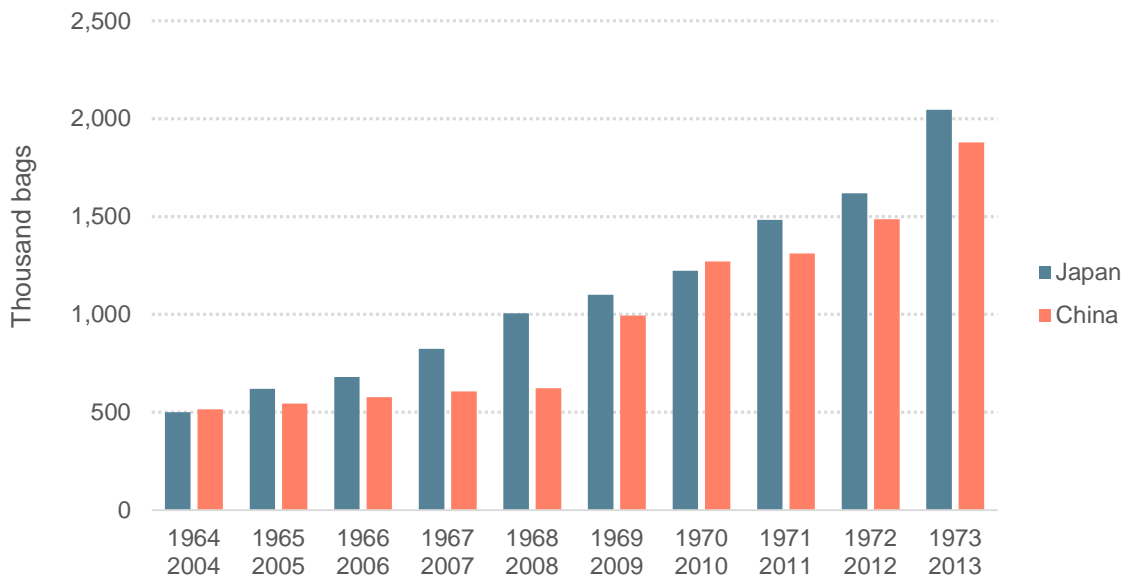
Figure 4: Origin of coffee imports by China (Average: 2009/10 to 2013/14)



Box 1: Coffee consumption in Japan

The development of the coffee industry in China over the last ten years is comparable to the evolution of coffee demand in Japan fifty years ago. As shown in figure 5 below, coffee consumption levels in China and Japan grew at similar rates over a ten-year period. Japan continued growing strongly until the mid-2000s when it reached over 7 million bags and became the world's fourth largest coffee consumer, with a per capita consumption of 3.5kg. Japan now has an advanced coffee culture, composed predominantly of Arabica and with a developed processing capacity. This process took 30 to 40 years in Japan, and China is still very much in the early stages of its coffee development.

Figure 5: Coffee consumption in China (2004/05 to 2013/14) compared to Japan (1964/65 to 1973/74)



III. COFFEE PRODUCTION IN CHINA

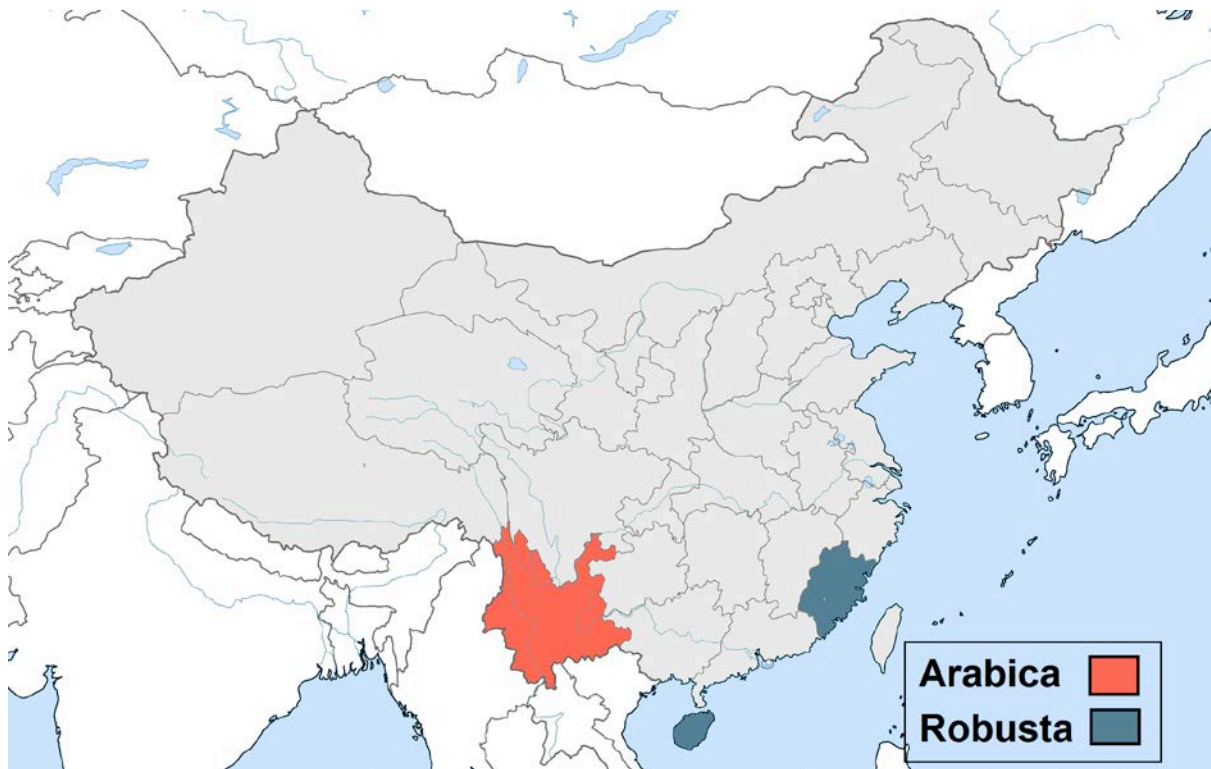
(a) History

8. Coffee was first introduced to China in the late nineteenth century by a French missionary in Yunnan province, in the southwest of the country. Coffee production subsequently languished for the better part of a century, until 1988 when the Chinese Government, in association with the World Bank and the United Nations Development Programme, initiated a project to regenerate the sector. Large companies like Nestlé also encouraged coffee growing in the region, and as a result production soared.

(b) Growing areas

9. Coffee is still predominantly grown in Yunnan province, which accounts for over 95% of China's coffee output. Yunnan is traditionally a tea-growing region, source of the renowned 'Pu'er' tea. However, with its mountainous landscape (an average altitude of around 2,000 metres) and mild climate it is well-suited to coffee production. It also borders Vietnam, Laos and Myanmar, in the heart of the coffee belt. It grows exclusively Arabica coffee, and is a large province with an area of 394,000 km² and population of 46 million people. There are also small amounts of Robusta grown on the island of Hainan, situated in south China, and in Fujian province, in the southeast.

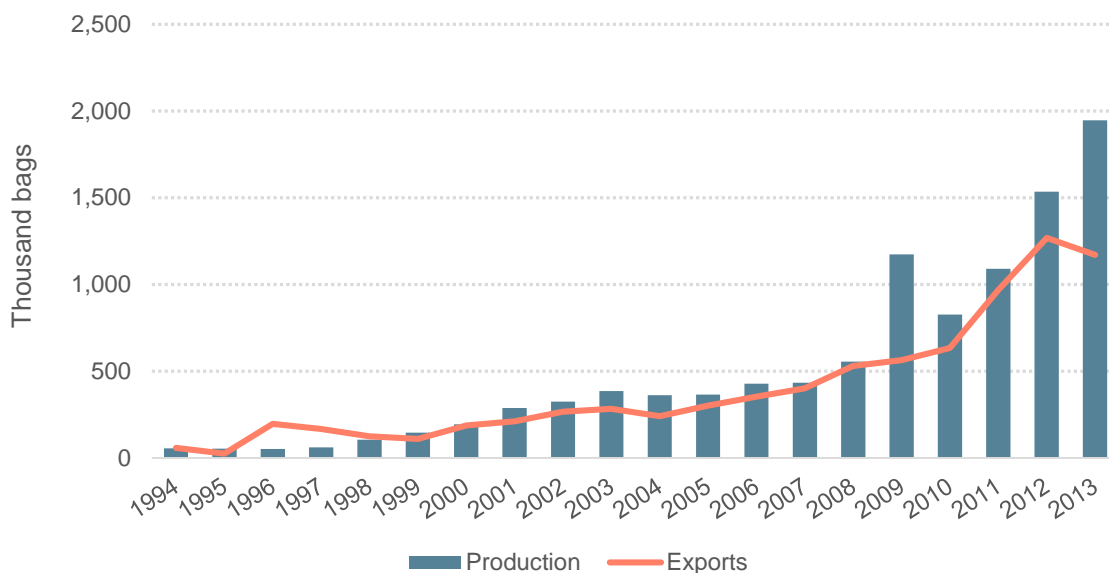
Figure 6: Coffee producing areas in China



(c) Current state of production (1994/95 to 2013/14)

10. Coffee production in China has escalated rapidly over the last twenty years (see figure 7). Figures from the Food and Agriculture Organization (FAO) suggest that output in crop year 2013/14 reached 1.9 million bags, and has been roughly doubling every five years. This would make China the 14th largest producer of coffee in the world, ahead of Costa Rica but behind Nicaragua, compared to the 30th worldwide ten years ago with a level of 361,000 bags.

Figure 7: Production and exports in China (1994/95 to 2013/14)



11. This growth in production has been encouraged by significant investment in the sector, from both the public and private sector (see Box 2). The Coffee Association of Yunnan has recently announced plans to invest RMB3 billion (US\$480 million) in coffee over the next ten years. This investment is to be used to improve soil quality, build research centres and provide training to coffee growers, expanding both the area of plantation and production.

12. Coffee production in Yunnan region has also been promoted by the decline in tea prices, making coffee significantly more remunerative. Farmers in the area can reportedly make double the income compared to tea over the same land area; farmers are also converting from maize or rice production because of the higher expected return.

13. There is some debate over the current quality of China's production. It is generally considered to fall short of specialty coffee standards, yet is too high to be used purely for local consumption. Most of the Arabica production is fully washed *Catimor*, although producers have recently been moving towards other varieties including *Typica* and *Bourbon*, which can bring a higher return.

Box 2: Private sector interest in China's coffee production

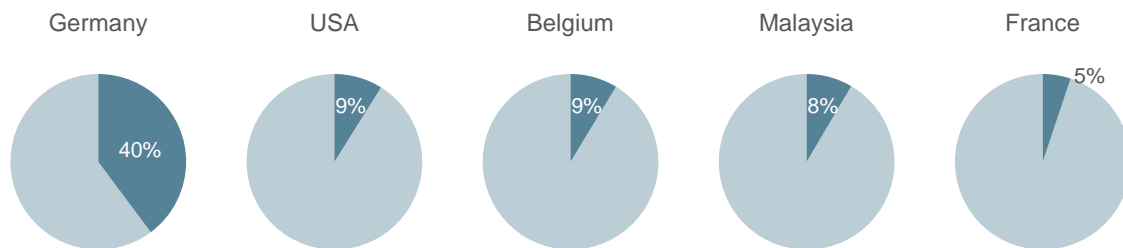
Private sector involvement in China's coffee production has also been growing recently. Nestlé has been present in Yunnan province since the late 1980s, but has significantly increased its purchasing and investment in the last few years. In 2013, Nestlé signed a memorandum of understanding with the local government of Pu'er to invest in a regional coffee centre. Starbucks has also been looking to expand its presence in the area, opening a farmer support centre in 2012 piloting the adaptation of alternative varieties with an emphasis on improving quality. Furthermore, in October 2014, the coffee trader Volcafe announced plans to partner with a local company, Simao Arabica Coffee Company, to source, process and export Chinese coffee beans to the international market.

(d) Exports

14. In parallel with its production levels, China's exports of coffee have been increasing sharply over the last twenty years. In absolute terms, from just 58,000 bags in 1994/95, China exported 1.2 million bags in 2013/14, nearly a twenty-fold increase. Around 90% of China's exports are in unprocessed, green form, with roast and soluble products averaging a 4% share each over the last five years.

15. In terms of destinations, over the last five years, China exported coffee to 97 different countries worldwide, although 71% of these shipments went to just five countries (see figure 8 below). Germany is by far the biggest destination, accounting for 40% of total exports over the last five years, where the coffee is likely processed and re-exported.

Figure 8: Destination of coffee exports by China (Average 2009/10 to 2013/14)



IV. PROSPECTS

16. The coffee sector in China is unsurprisingly generating significant interest; the extraordinary growth exhibited in both production and consumption has the potential to alter the coffee landscape in unpredictable ways. Based on official government statistics and derived figures, production is estimated at just over 1.9 million bags and consumption at just under 1.9 million, with both growing at double-digit rates. It should, however, be noted that these estimates are significantly higher than other sources, which range between 1.1 and 1.5 million bags. This could be explained by increasing consumption of domestically produced coffee, but suggests that all figures should be treated somewhat carefully.

17. Returning to the comparison with the development of the coffee sector in Japan, consumption in China could follow a similar growth trajectory. Coffee consumption in Japan has stabilised recently at a level of just over 7 million bags, or 3.5kg per capita. China has a population ten times larger than Japan, although coffee is predominantly consumed in the urban areas which cover around half of the total population. By the end of the decade, China could be consuming over 4 million bags per year, with plenty of potential for further growth.

18. Similarly, Arabica production in Yunnan province has been growing substantially, and the Coffee Association of Yunnan has set a target of 4 million bags by 2020. Furthermore, looking at the import/export statistics for China suggests that an increasing proportion of local production is being consumed internally. This trend fits the narrative that companies involved in both supply and demand in China, such as Nestlé and Starbucks, are increasingly investing in Chinese coffee production in order to supply the local market with specifically targeted blends and products. As the preference for Arabica in China continues to rise, this pattern looks likely to continue.

19. To conclude, the overall impact of the Chinese coffee sector on the global coffee economy is as yet undetermined. By driving up both production and consumption in relatively proportional amounts, China is currently a broadly neutral presence on the global balance sheet. However, the dynamics of these two trends are very different, with production composed almost entirely of Arabica coffee and consumption currently favouring Robusta. A more in-depth analysis of these trends would be facilitated by more data.

DATA AND METHODOLOGY

The availability of data on coffee in China has presented some problems in terms of analysing trends and dynamics. The numbers used in this report were calculated as follows:

1. Import and export data: these numbers are made available to the ICO through customs statistics, which cover imports and exports into mainland China, and the official statistics offices of Hong Kong and Macao, which are then aggregated.
2. Production: statistics on coffee production in China are available from the Food and Agriculture Organization of the United Nations (FAO). These are given in tonnes, which were then converted into 60kg bags.
3. Consumption: No consistent data on consumption were found. Therefore, these numbers were derived by calculating *Production + Imports - Exports*, and then a rolling two-year average was used to smooth out any unusual year-to-year changes. This approach also assumes zero changes in stock levels over time.

This data was calculated over a twenty year period from crop year (October to September) 1994/95 to 2013/14. Full data can be seen in the table below.

Table 1: Coffee statistics for China

	Production	Consumption	Exports	Imports
1994/95	54	180	58	173
1995/96	53	255	24	313
1996/97	50	220	196	245
1997/98	60	109	166	225
1998/99	104	167	124	236
1999/00	146	245	109	238
2000/01	193	282	186	282
2001/02	287	337	212	309
2002/03	324	396	265	348
2003/04	386	448	283	387
2004/05	361	514	240	418
2005/06	365	544	301	485
2006/07	428	576	352	527
2007/08	433	606	401	577
2008/09	555	623	530	611
2009/10	1 173	994	563	742
2010/11	827	1 271	633	995
2011/12	1 090	1 312	969	1 314
2012/13	1 534	1 488	1 269	1 275
2013/14	1 947	1 891	1 170	1 463
Growth rates				
1994-2013	21%	13%	17%	12%
2004-2013	21%	16%	19%	15%

In thousand 60kg bags