



CHINA DAIRY REPORT



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SUMMARY



China's demand for imported dairy products will not diminish in the short-term. Consumption of dairy products in this highly populated country is growing extremely rapidly. The current short-fall in domestic milk supply in China is anticipated to continue. There is huge potential in China for incredible growth in milk output in the coming years.

China is perhaps the only country in the world with the finance, ambition and ruthlessness to achieve their desired growth in milk output. However the people of China are now demanding much higher food safety standards. The 2008 melamine crisis and subsequent food safety violations means the population are scared of consuming locally produced dairy products. The ability of China to increase milk production is constrained by quality demands.

Dairy products are not a traditional food for the Chinese. That said, consumption of milk is considered to be good for health. The main uptake of liquid dairy products is by those with greater nutritional requirements, mostly young children and the elderly.

Increased wealth, an expanding population, and urbanization are all driving consumption of dairy products. The proportion of the population living in extreme poverty is declining. In 2007 it was estimated that 10% of the Chinese population were living below the poverty line. Now it is estimated that just 2.8% of the population have an annual income below US\$90 per annum.

China is the most populous country in the world with 1.3 billion people. Approximately half of the population now live in cities. Urbanisation is expected to continue in the coming years with 30 million people relocating from the rural areas to the cities each year. They are being attracted by higher incomes and the opportunity to improve their living conditions. At present there are three cities in China with a population greater than 10 million. These cities are Shanghai, Beijing, and Guangzhou. By 2025 there are expected to be 8 cities with a population greater than 10 million and 221 cities with a population over 1 million.

China is the most populated country in the world, but its rate of growth is slowing. The birth rate is much in line with that of developed countries. 2011 estimates put the birth rate in China in line with that of Australia, France and the United Kingdom. Due to China's vast population this still means approximately 16 million babies are born in China every year. The "one child policy" does not universally apply across China. The birth rate in 2011 is estimated to be 1.54 children born per women. There are many exceptions to the "one-child" policy. Family planning limitations are managed at the provincial level so actual policies and enforcement vary within China.

Milk production growth was similar rate to the growth in dairy product consumption until 2008. The high demand for dairy products ultimately led to the melamine milk contamination scandal in 2008. Melamine was added to milk to artificially increase the protein readings after the milk had been watered down. Since this time authorities have had to deal with conflicting demands of increased milk quantity and higher milk quality. The trade off has resulted in a gap occurring between the quantity of product supplied by the Chinese domestic market and the volume of dairy products demanded. Imported dairy products have since filled this gap.

The Chinese dairy industry is currently going through a period of rapid change. Processing facilities are being upgraded and milk collection procedures have been tightened. The industry has the potential to produce large quantities of high quality milk. There are however many factors which will limit the milk output in the medium term. These include the lack of water resources and the priority for food crops over feed crops. This means feed for dairy cows needs to be imported and as a consequence the cost of producing milk in China is relatively high. There is also a lack of skills required to manage the large scale intensive dairying operations that are currently being developed.

The factors limiting milk output in China are being addressed and will eventually be conquered. China's ability to implement change is incredible and should not be underestimated. However the one factor that will take time rather than money to fix is the lack of consumer confidence in local dairy produce.

NZX Agrifax predicts the demand for imported products will remain strong in the coming years. A gap has opened up between the volume of milk required to meet consumer demand and the quantity the domestic dairy industry can deliver. We do not expect this gap to erode in the near future.