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Global Agricultural Information Network

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Report Highlights:

Post estimates that China's 2014 fluid milk production will decline by three percent to 36 million tons due to herd reductions and stricter regulations on dairy/infant formula production. Strong consumer demand will continue to support record imports of fluid milk, non-fat dry milk powder and whole milk powder. Post's 2014 fluid milk import figure remains unchanged at a record high of 300,000 tons. Imports of non-fat dry milk powder and whole milk powder are estimated at 330,000 tons and 900,000 tons, respectively. Given tight domestic supplies and high export prices, China's exports are likely to decline to leading markets.

Executive Summary:

Post reduced its estimate for China's 2014 fluid milk production by three percent to 36 million tons. China's stricter domestic requirements for dairy/infant formula milk production are expected to reduce supplies by some small-scale producers. Post's 2014 fluid milk imports remain unchanged at 300,000 tons; meanwhile, exports are lowered by 12 percent to 22,000 tons because of weak demand in Hong Kong and Myanmar. In 2013, small-scale dairy producers slaughtered low producing 'cows in milk' to take advantage of favorable beef prices.

China's 2014 nonfat dry (NFD) milk production is estimated to fall four percent to 49,000 tons because of limited domestic raw milk supplies. NFD is not a traditional dairy product in China, and imports can satisfy domestic demand. Post estimates that China's 2014 NFD imports will reach 330,000 tons, 32 percent higher than USDA's official forecast. Sources note that NFD milk imports are becoming a substitute for whey imports due to price competitiveness.

Post estimates that China's 2014 whole milk powder (WMP) production will decline by four percent to 1.25 million tons; however, imports will support a WMP consumption increase to 2.15 million tons. Similar to NFD, part of WMP is used as a base powder material for infant formula productions. China's stricter requirements for imported infant formula milk powder as of May 2014 will allow major Chinese domestic plants to expand infant formula milk powder production by importing more NFD and WMP as base powder material. Therefore, Post estimates China's 2014 WMP imports at 900,000 tons, a 28 percent increase over USDA's official forecast.

Note: Infant formula production and imports are not included in the whole milk and non-fat dry powder PS&D tables.

Commodities:

Dairy, Milk, Fluid

Dairy, Milk, Nonfat Dry

Dairy, Dry Whole Milk Powder

Fluid milk PS&D table

Dairy, Milk, Fluid China	2012		2013		2014		
	Market Year Begin: Jan 2012		Market Year Begin: Jan 2013		Market Year Begin: Jan 2014		
	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post	
Cows In Milk	8,000	8,000	8,380	8,350	8,900	8,710	(1000 HEAD)
Cows Milk Production	32,600	32,600	34,500	34,300	37,000	36,000	(1000 MT)
Other Milk Production	1,360	1,360	1,450	1,450	1,550	1,500	(1000 MT)
Total Production	33,960	33,960	35,950	35,750	38,550	37,500	(1000 MT)
Other Imports	94	94	180	185	300	300	(1000 MT)
Total Imports	94	94	180	185	300	300	(1000 MT)
Total Supply	34,054	34,054	36,130	35,935	38,850	37,800	(1000 MT)
Other Exports	27	27	25	25	25	22	(1000 MT)
Total Exports	27	27	25	25	25	22	(1000 MT)
Fluid Use Dom. Consum.	13,517	13,517	14,350	14,350	15,460	15,150	(1000 MT)
Factory Use Consum.	20,510	20,510	21,755	21,560	23,365	22,628	(1000 MT)
Feed Use Dom. Consum.	0	0	0	0	0	0	(1000 MT)
Total Dom. Consumption	34,027	34,027	36,105	35,910	38,825	37,778	(1000 MT)
Total Distribution	34,054	34,054	36,130	35,935	38,850	37,800	(1000 MT)
CY Imp. from U.S.	0	0	0	4	0	6	(1000 MT)
CY. Exp. to U.S.	0	0	0	0	0	0	(1000 MT)
TS=TD		0		0		0	

(New Post estimates are not official USDA data. Official USDA data is located at <http://www.fas.usda.gov/psdonlineonline>)

Production

Post lowered its estimate for China's 2014 fluid milk production to 36 million tons, a decrease of three percent to USDA's official forecast. Small-scale dairy producers' compliance with China's stricter requirements on local milk production is expected to result in fewer supplies. Post finalized its China 2013 fluid milk production figure at 34.3 million tons, a one percent decrease from USDA's official estimate, due to a fewer-than-expected number of 'cows in milk'. Small-scale dairy producers slaughtered low producing animals to take advantage of favorable beef prices which were up by 30 percent in 2013.

China's 2013 average farm gate milk price (year-on-year) increased by 10 percent to RMB 3,745 (\$604) per ton. Dairy producers are increasingly paying attention to animal feed nutrition to improve yields and capitalize on higher milk prices. China's abundant 2013-14 grain/grass harvests and alfalfa imports played a role in improved milk yields.

Post's most recent assessment on China's grain and feed situation can be viewed at.

http://gain.fas.usda.gov/Recent%20GAIN%20Publications/Grain%20and%20Feed%20Annual_Beijing_China%20-%20Peoples%20Republic%20of_4-2-2014.pdf.

Inner Mongolia: the Home to China's Dairy Industry

Land, capital, and technology resources remain major challenges for small-scale dairy producers in Inner Mongolia, China's largest dairy production province. As a result, in some areas of this province, small-scale producers rent their cows for five years to large dairy companies through the Dairy Union, a well-known local entity. At the end of this term, the large dairy company returns the rented cows and keeps the calves borne during the rental period. This model is one of several approaches to help Inner Mongolia increase its dairy herd by 20 percent to 500,000 head. Dairy is a key industry in Inner Mongolia, so in 2014, the local government allocated RMB60million (\$9.68 million) to support local processing plants that established partnerships with at least 30 percent of nearby backyard cow producers. This allocated funding is also used to support the formation of local cooperatives by small operators.

China's large domestic dairy companies are building partnerships with foreign entities to help improve productivity which could include plans for new facilities in East and North China areas.

Prices

With continuing strong fluid milk demand and limited domestic supplies and resources, China's first quarter 2014 milk market price rose by 19 percent over 2013 to \$684 per ton. Higher feed,-labor and transportation costs were major factors in milk price increase. Regarding feed costs, sources noted differences in transportation fees for imported and domestic products. For instance, transportation fees for imported U.S. alfalfa to Shanghai (in East China) can range from \$45-\$65 per ton, whereas local transportation fees for domestic alfalfa from Gansu Province (in Northwest China) to Shanghai can be four times higher at \$194 to \$242 per ton.

Consumption

Post lowered its forecast for China's 2014 fluid milk consumption by three percent to 37.7 million tons due to lower-than-expected domestic supplies. Similar to 2014, Post reduced its 2013 figure by three percent to 35.9 million tons.

Trade

Imports:

Post's estimate for China's 2014 fluid milk imports remains unchanged at 300,000 tons. Strong consumer demand and tight domestic supplies are expected to continue as are high import prices. The first quarter 2014 import price increased by five percent to an average of \$1,280 per ton. During the same period, the import price for China's largest fluid milk supplier, Germany, increased by 19 percent to \$1,023 per ton. Despite the price rise, German products remain price competitive compared with other major competitors, accounting for nearly 40 percent of China's total imports in the first quarter.

U.S. fluid milk exports to China are improving due to newly branded products. Almost all imported fluid milk is ultra-high temperature (UHT) milk for first-tier and second-tier Chinese cities. Nearly 40

percent of China's fluid milk imports are distributed through online shops, while the remaining 60 percent is mainly distributed through supermarkets/hypermarkets.

Post revised its China's 2013 import figure to 185,000 tons based on available trade data.

Alfalfa: China's Rising Dairy Feed Ingredient [Harmonized System (HS) Code: 121490]

Post estimates that China's 2014 alfalfa imports will increase over 26 percent to nearly 1 million tons. In the first quarter of 2014, China's alfalfa imports increased y-o-y by 26 percent to 188,087 tons which is valued at more than \$68 million. The United States is the largest supplier to China, accounting for 90 percent of total imports. To help build domestic supplies, China's Ministry of Agriculture plans to invest RMB 300 million (\$5 million) a year to develop 33,000 hectares of alfalfa demonstration production bases.

Exports:

Post lowered its forecast for China's 2014 fluid milk exports to 22,000 tons, a decrease of 3,000 tons or 12 percent below USDA's official forecast, because of weakened demand in Hong Kong. Hong Kong is China's largest export market for fluid milk, accounting for 97 percent.

Nonfat dry PS&D table

Dairy, Milk, Nonfat Dry China	2012		2013		2014		
	Market Year Begin: Jan 2012		Market Year Begin: Jan 2013		Market Year Begin: Jan 2014		
	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post	
Beginning Stocks	0	0	0	0	0	0	(1000 MT)
Production	57	57	54	54	51	49	(1000 MT)
Other Imports	168	168	215	235	250	330	(1000 MT)
Total Imports	168	168	215	235	250	330	(1000 MT)
Total Supply	225	225	269	289	301	379	(1000 MT)
Other Exports	0	0	1	0	1	0	(1000 MT)
Total Exports	0	0	1	0	1	0	(1000 MT)
Human Dom. Consumption	225	225	268	289	300	379	(1000 MT)
Other Use, Losses	0	0	0	0	0	0	(1000 MT)
Total Dom. Consumption	225	225	268	289	300	379	(1000 MT)
Total Use	225	225	269	289	301	379	(1000 MT)
Ending Stocks	0	0	0	0	0	0	(1000 MT)
Total Distribution	225	225	269	289	301	379	(1000 MT)
CY Imp. from U.S.	18	18	47	53	54	79	(1000 MT)
CY. Exp. to U.S.	0	0	0	0	0	0	(1000 MT)
TS=TD		0		0		0	

(New Post estimates are not official USDA data. Official USDA data is located at <http://www.fas.usda.gov/psdonlineonline>)

Production:

Post reduced its estimate for China's 2014 non-fat dry (NFD) milk powder production by four percent to 49,000 tons. NFD is not a traditional dairy product in China, and imports can satisfy domestic demand. Processors will use available raw milk supplies to produce higher-priced infant formula milk powder, instead of NFD milk powder. NFD is not a traditional dairy product in China. Given less

domestic NFD production, Post estimates larger imports for China's dairy processing. Please see the Import Section below.

Consumption:

Post's estimate for China's 2014 NFD consumption is revised to 379,000 tons, an increase of 26 percent. Some domestic plants are expanding their infant formula milk powder production by using imported NFD as a processing material and as whey substitute.

Imports

Strong domestic demand and lower-than-expected domestic milk production is expected to support Post's 2014 import estimate, despite higher import prices. Post increased its China 2014 NFD import figure by 32 percent to 330,000 tons. New Zealand currently dominates China's NFD imports, accounting for more than 50 percent. In the first quarter in 2014, China's import price for U.S. NFD powder was \$4,311 per ton, while the New Zealand price was \$4,804 per ton. Sources note that China's first quarter imports are normally high because Chinese importers want to complete their import quotas at low tariffs within the China-New Zealand bilateral Free Trade Agreement. On the contrary, the New Zealand market share is challenged by U.S. exports to China. The U.S. 2013 NFD market share in China reached 23 percent from 11 percent in 2012. Moreover, the U.S. export price to China averaged \$3,984 per ton compared to New Zealand's export price of \$4,130.

Post finalized its China's 2013 NFD imports at 235,000 tons based on official trade data.

Whole milk powder PS&D table

Dairy, Dry Whole Milk Powder China	2012		2013		2014		
	Market Year Begin: Jan 2012		Market Year Begin: Jan 2013		Market Year Begin: Jan 2014		
	USDA Official	New Post	USDA Official	New Post	USDA Official	New Post	
Beginning Stocks	50	50	60	60	30	0	(1000 MT)
Production	1,160	1,160	1,220	1,200	1,300	1,250	(1000 MT)
Other Imports	406	406	535	619	650	900	(1000 MT)
Total Imports	406	406	535	619	650	900	(1000 MT)
Total Supply	1,616	1,616	1,815	1,879	1,980	2,150	(1000 MT)
Other Exports	9	9	5	3	5	2	(1000 MT)
Total Exports	9	9	5	3	5	2	(1000 MT)
Human Dom. Consumption	1,540	1,540	1,777	1,876	1,975	2,148	(1000 MT)
Other Use, Losses	7	7	3	0	0	0	(1000 MT)
Total Dom. Consumption	1,547	1,547	1,780	1,876	1,975	2,148	(1000 MT)
Total Use	1,556	1,556	1,785	1,879	1,980	2,150	(1000 MT)
Ending Stocks	60	60	30	0	0	0	(1000 MT)
Total Distribution	1,616	1,616	1,815	1,879	1,980	2,150	(1000 MT)
CY Imp. from U.S.	0	2	2	6	3	7	(1000 MT)
CY. Exp. to U.S.	0	0	0	0	0	0	(1000 MT)
TS=TD		0		0		0	

(New Post estimates are not official USDA data. Official USDA data is located at <http://www.fas.usda.gov/psdonlineonline>)

Production

Post lowered its estimate for China's 2014 whole milk powder (WMP) production by four percent to 1.25 million tons. This reduction is attributed to China's smaller-than-expected pace of growth in domestic milk production and stricter policy for dairy/infant formula milk powder production. Sources note that small-scale processors may not pass China's re-verification and re-registration for production permit by the end of May 2014 required by China's Food and Drug Administration (CFDA). If a large number of processors become ineligible, then domestic WMP supplies would be further strained.

Post finalized its estimate for China's 2013 production at 1.2 million tons, a two percent decline from USDA's official figure, because of smaller-than-expected raw milk supplies.

Consumption

Post increased its China 2014 WMP consumption by nine percent to 2.1 million tons. This revision is largely due to imports used for base powder material in infant formula milk powder production and reconstitution for yogurt production, beverage drinks, and food processing.

Post finalized its 2013 consumption estimate by five percent to 1.88 million tons.

Trade

Imports:

Although China's WMP domestic production has grown moderately over the past few years, imports have significantly contributed to rising domestic demand. Post increased its China 2014 WMP import estimate by 28 percent to 900,000 tons because of limited domestic supplies, tightened government regulations, and rising consumer demand. Several factors can explain significantly higher imports in 2014.

- 1) By completing the registration process from China's National Certification and Accreditation Administration (CNCA) by May 1, 2014, registered foreign companies are permitted to export infant formula milk powder to China. With this public list of registered companies, all Chinese processing plants can offset their losses due to limited domestic dairy/infant formula production by importing NFD and WMP products for further processing into base powder material.
- 2) Sources note that dairy/infant formula products will continue to benefit from low tariffs under the China and New Zealand Free Trade Agreement (FTA). After China and New Zealand signed the FTA, New Zealand's WMP exports to China went from 32,471 tons in 2008 to 562,604 tons in 2013.
- 3) On March 18, 2014, China and New Zealand announced a joint agreement to allow China's currency (Renminbi (RMB)) to be directly traded with New Zealand Dollars.
- 4) Given China's strong domestic demand and limited WMP supplies, China's 2013 imports were more than 50 percent of China's domestic production. Post estimates that China's 2014 WMP imports will reach 72 percent of China's domestic production.

Post finalized its 2013 WMP import figure at 619,000 tons, a 16 percent increase over higher than USDA's official forecast, based on official trade data.

Exports

Post lowered its forecast for China's 2014 WMP exports to 2,000 tons, a decrease of 60 percent from USDA's official forecast, due to weak export demand in leading markets, such as Hong Kong and Myanmar, which account for 75 percent of China's total exports. Reportedly, weak demand in Hong Kong is due to product safety concerns. China's higher export prices attribute to lower sales in Myanmar. This year, given China's short domestic supplies, its first quarter export price to Myanmar grew by 47 percent to \$6,435 per ton from same period in 2013.

Update of Infant formula milk powder Harmonized System (HS) Code: 19011010

To work towards regaining consumer confidence in domestic infant formula milk powder, the Chinese government created and revised several policies in 2013 and 2014. Please review Post's comprehensive list of China's 2013 Dairy Regulations (as of February 2014) at this link:

http://gain.fas.usda.gov/Recent%20GAIN%20Publications/China's%202013%20Dairy%20Regulations/Beijing_China%20-%20Peoples%20Republic%20of_2-10-2014.pdf

Since the release of this report, China has issued additional regulations:

The Chinese 2014 Customs Yearbook for Import and Export Tariffs announced the 8-digit HS Code 19011010 for infant formula milk powder and HS Code 19011090 for other infant formula dairy products. [Note: During the first quarter of 2014, infant formula imports rose by 14 percent to 29,342 tons and valued at \$363 million.]

At the National People's Congress meetings in March, China announced its new family planning policy, which allows married couples to have a second child, if one of the parents is a single child.

As of April 1, China's Food and Drug Administration permits domestic infant formula milk powder processing plants to use imported base powder as a processing material. These plants must process in accordance with the requirements under the Base Powder Definition in CFDA's Detailed Regulation on Verification of Infant Formula Production Permit. Furthermore, plants are not allowed to import large bags of infant formula milk powder and repack them into small-retail packages. If plants purchase imported base powder, Chinese competent authorities will verify the qualifications of the importers or agents.

Also, on April 1, the General Administration of Quality Supervision, Inspection and Quarantine requested that imported infant formula milk powder must have labels in Chinese. All labels must be printed on retail-size packages before entering China, and applying labels onto packages after entering China is no longer accepted. According to AQSIQ, shipments that do not comply with these requirements will be returned or destroyed.

China's National Health and Family Planning Commission requires that, when an infant formula production permit expires or needs to be replaced, the plant's production permit must be re-verified. In China, all infant formula plants must be verified by May 31. Plants that pass the verification process must submit their product ingredients, packaging and labeling designs to their Provincial Health and Family Planning Commission. If plants do not obtain a new permit by May 31, the plant's production permit will be suspended; however, China will issue a two-year corrective period.

Other Dairy Products

Whey: China's 2014 whey imports are trending downward partly due to higher import prices. This year, the first quarter U.S. import price climbed 15 percent to \$1,489 per ton compared to the same period in 2013. Sources note that China's total 2014 whey imports may fall by two percent to 422,000 tons. In addition to high import prices, U.S. exports are also constrained by whey powder use in China. Although low protein whey powder is allowed for food processing in the United States, low-protein whey can only be used for feed in China. The United States is the largest whey supplier to China.

Cheese: China is a net cheese importer. China's 2014 cheese imports are forecast at 72,400 tons, a 53 percent increase from the previous year due to strong domestic demand and Chinese consumers' dietary change. Continued popularity of pizza and western fast-food chained restaurants will drive consumption and imports. New Zealand, Australia and the United States are the top three suppliers, accounting for almost 88 percent of China's total imports. U.S. 2014 exports to China are forecast to rise 16 percent to 11,600 tons due to competitive prices. Although U.S. 2014 export price climbed six percent in the first quarter, it was still \$439 lower than the New Zealand price and \$188 lower than the Australian price for China's market.

On April 26, 2014, Mengniu and Danish Arla Foods established a joint China-Denmark Milk Technology Cooperation Center/Arla Innovation Center China, a first national research center in China. One of the Center's main objectives is to develop cheese products suitable for the Chinese consumer diet and to help more Chinese understand its nutritional benefits.