



China: 3 trends driving the food and beverage industry



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As China pursues its “dual circulation” growth strategy in the coming decade, domestic consumption will be the most important pillar. This presents investment opportunities in the food and beverage industry. New trends and changing consumer preferences are benefitting brands that focus on health, convenience and innovation.

China’s food and beverage (F&B) market is fast-growing. In 2021, revenue is expected to hit US\$176bn which makes up 63% of the global F&B revenue. Looking ahead, the annual revenue growth rate is projected at 8.38% between 2021 and 2025¹.

We think these are the three areas that are driving change and growth in the F&B industry. F&B brands that actively build a high-end image and launch differentiated high-end products have an edge over competitors.

ONGOING CONSUMPTION UPGRADE

China’s consumption upgrade trend is not a new one with consumers in high tier cities buying

premium and luxury products and services whilst those in the lower tier cities are choosing more branded products. While the COVID-19 pandemic would have dampened spending to some extent, the trend is still present and increasing. The F&B industry is experiencing a similar pattern. Affluent and informed Chinese consumers have begun to prioritise better health and a better quality of life. As a result, products aligned with healthier lifestyles have seen increased demand.

This is evident across the beverage industry. The packaged drinking water is the biggest beverage segment in China’s soft beverage market. While purified drinking water has a majority share of this segment, natural water and natural mineral water have grown the fastest in recent years as a result of growing health consciousness. Likewise, less or no sugar teas, cleansing juices and nutritional drinks have all experienced higher demand in recent years.

Turning to food, a survey reveals that 86% of consumers from tier 1 and tier 2 cities consider food safety before buying the food². Fresh food such as vegetables, eggs, meat and fruits, is one food category that is high in demand as it is

considered natural and free from chemicals. In line with this, another area that is seeing growth is that of natural healthy packaged food such as salads.

While health and safety play a key role in consumers' F&B preferences, there is also an emphasis on the fulfilment one gets from consuming premium brands. Relating to alcoholic beverages, consumers are now placing more value on experience and enjoyment and hence prepared to pay more for products that fulfil this need. Premium baijiu is expected to deliver superior growth in 2021 and onwards whilst premiumisation is the predominant driver behind Chinese beer brewers' profit growth. Fig 1 shows that the premium beer segment volume is expected to trend up.

Companies that offer a comprehensive and premium range of products which focus on the "authentic, natural, healthy and quality" themes

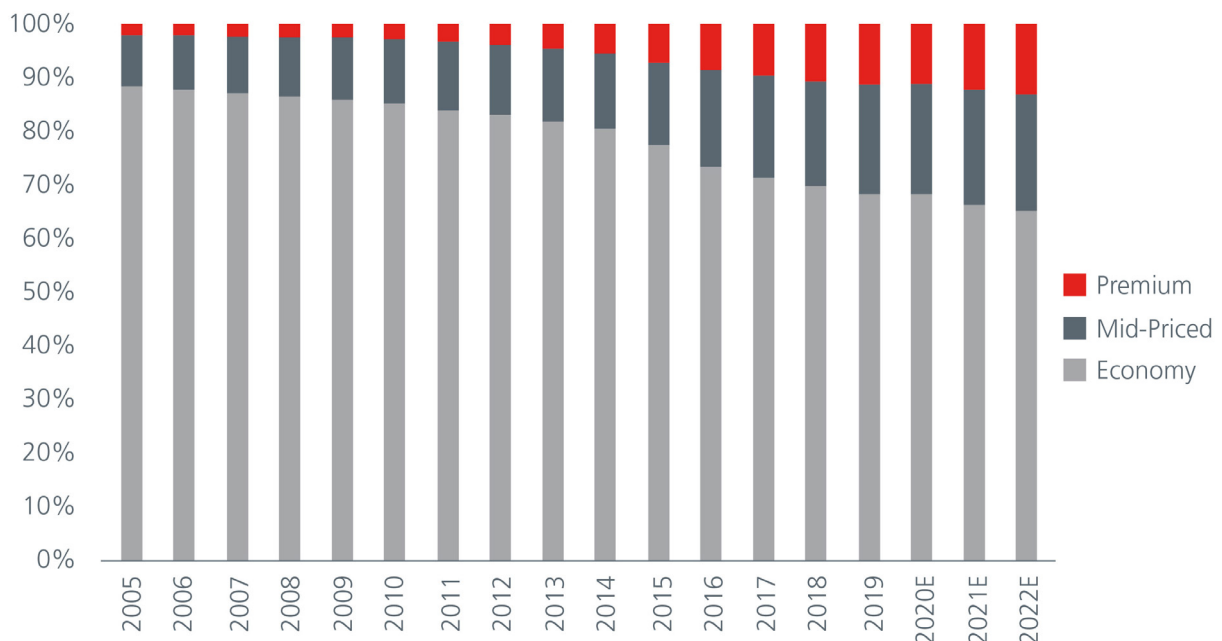
are in the sweetest spot for catering to Chinese consumers' premiumisation demand in the F&B segment.

THE RISE OF THE ONLINE GROCER³

Like the consumption upgrade trend, online shopping is not a new development. Rather the pace of its adoption amongst consumers has accelerated following the COVID-19 induced lockdowns. E-commerce is now a vital part of consumer shopping behaviour in China, with a penetration rate of 30% as of end 2020.

The e-grocery (fresh produce and fast-moving consumer goods) rate however has lagged at 10% penetration and this is likely due to the short shelf life nature of fresh food which puts demand on logistics, as well as offline channels such as convenience stores that cater to on-demand items. Nonetheless the online habits acquired since the

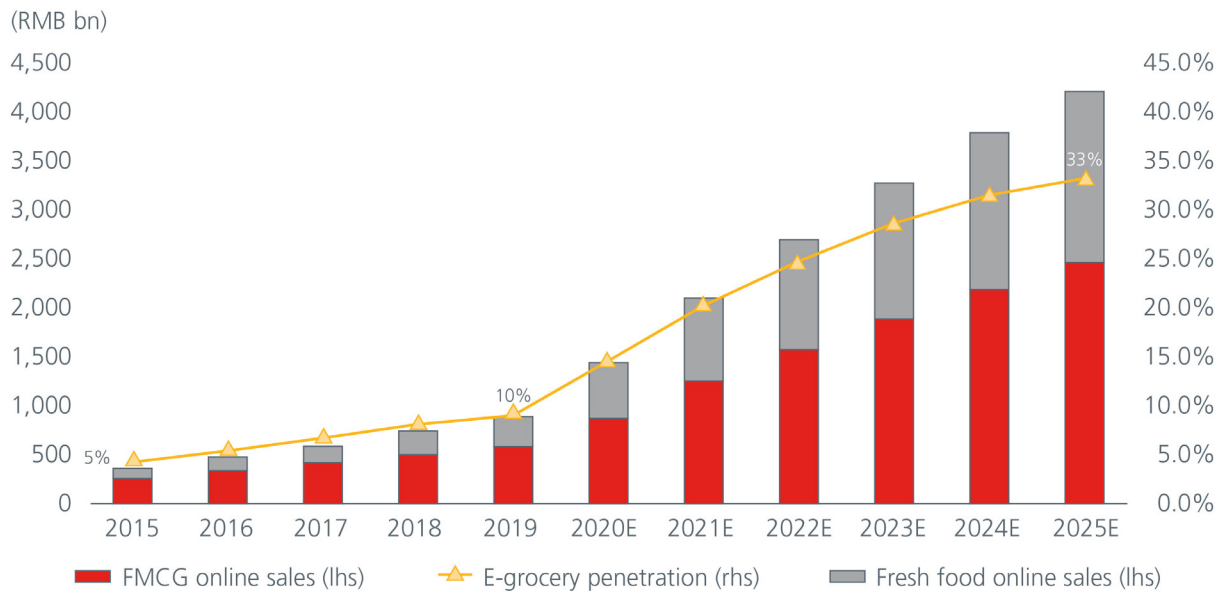
Fig. 1: Beer market segment mix (in terms of volume)



Source: Euromonitor, Credit Suisse estimates.

Source: ³All data references in this section come from the Credit Suisse report on China e-commerce and Consumer Sectors, Dec 2020.

Fig. 2: E-grocery market forecast



Source: Euromonitor, Credit Suisse estimates.

pandemic, improved infrastructure & distribution channels plus brands shifting online are expected to accelerate e-grocery penetration rates to 33% in 2025. See Fig 2.

Convenience and quality are driving the digitally savvy younger consumers to purchase groceries online. And it is not just consumers in tier 1 and 2 cities that are doing so, shoppers in tier 3-5 cities are also embracing this shift and are expected to contribute to more than half of the increment in the e-grocery market size between 2019 -2025.

INNOVATIVE PRODUCTS IN DEMAND

Innovation in F&B is becoming more important with new products, new packages, new channels and new ways of marketing to capture consumers. In the beverage drink segment, companies have been continuously coming up with new product launches to cater to younger consumers.

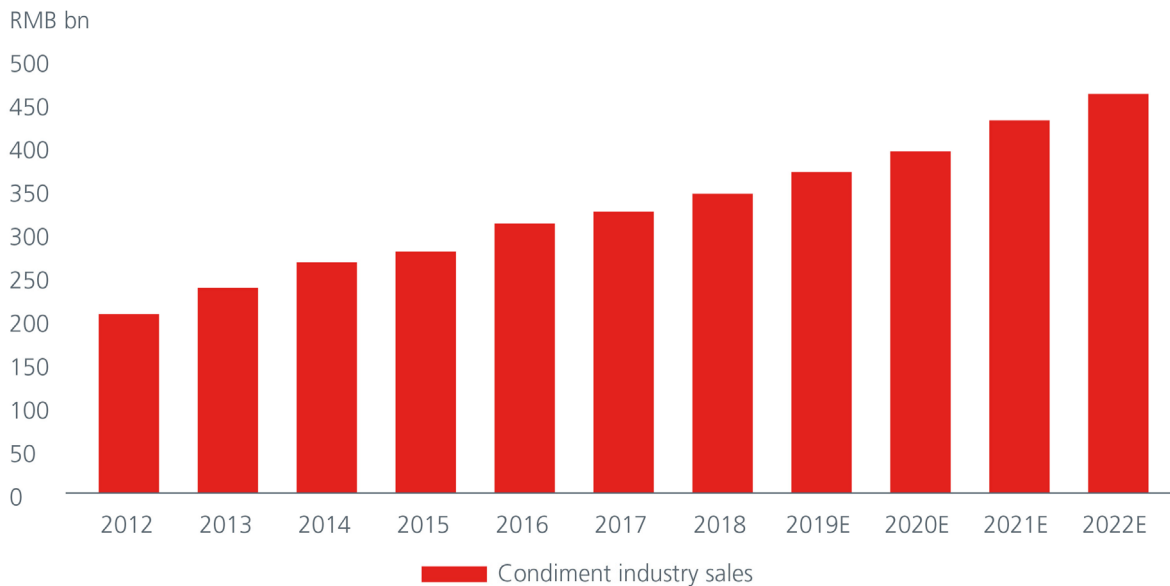
Likewise, China’s local condiment players have been launching various customised and functional products to meet the different cuisine demands

of consumers. For example, in soy sauce, there are customised ones for clay pot, Hainanese chicken and steamed fish. The retail prices of these could be more than double those of ordinary products. See Fig 3.

Innovative packaging is another area that is driving sales; a leading Chinese beverage manufacturer has seen strong volume growth of its packaged drinking water products owing to creative packaging. Technology is also playing a huge role in helping innovation. The popularity of live streaming in China has helped many new product launches whilst instagrammable foods and experiences appeal to the younger consumers.

Likewise, online live broadcasting and direct to customer (DTC) online sales channel have become popular and efficient ways to reach consumers for brand building, and marketing and sales, especially for emerging brands. The rich data online on consumer preferences and behaviour has provided companies with enormous insights on how to utilise them.

Fig. 3: Condiment industry sales



Source: NBS, Credit Jefferies estimates.

PLENTY OF ROOM FOR GROWTH

Based on 2019 World Bank data, China's final consumption as a proportion of its gross domestic product stood at 56%, a low number compared to the 81.8% in the US. According to a recent Morgan Stanley report, Chinese consumer spending is set to more than double in 10 years, with an emphasis on services rather than goods. By 2030, China's private consumption is set to reach US\$12.7 trillion, about the same amount that American consumers currently spend⁴.

In terms of F&B categories, we believe that premium alcoholic drinks, yogurt and fresh dairy, innovative compound condiments, packaged drinks, and health supplements will experience above average growth rates. That said, we see investment opportunities in brands that build a

premium story, in companies that offer healthy choices and utilise innovative channels to do marketing and in e-commerce platforms and e-grocery enablers.

This is the fifth of six articles in Eastspring's 2021 Asian Expert Series. In this new series which focuses on China, our investment teams offer insights into the opportunities and challenges facing China as it rolls out its 14th Five-Year Plan.

Click [here](#) to read other articles in our Asian Expert Series.

Source: ⁴<https://www.cnbc.com/2021/01/29/chinese-consumer-spending-to-double-by-2030-morgan-stanley-predicts.html>

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