



Exporting Fresh Fruit and Vegetables to China

A MARKET OVERVIEW AND GUIDE
FOR FOREIGN SUPPLIERS

Exporting Fresh Fruit and Vegetables to China A Market Overview and Guide for Foreign Suppliers

prepared by

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References and Data Sources:

Statistics presented in this report come from various sources including presentations and reports by industry experts, governmental and non-governmental research publications, academic sources, and corporate websites. Please direct inquiries regarding reference lists and/or data sources to the author at info@mzmc.com.cn.

1. Introduction

1.1 China's Economic Environment

Although China's economy grew by its slowest rate since 1990, with GDP growth for 2015 measuring at 6.9% and missing official Chinese targets of yearly minimum increases of 7.5%, many analysts are attributing this not to a serious slowdown of the Chinese economy. Rather, they point to the restructuring of China's economic developmental patterns away from the volatility of a fast-growth environment and toward a more sustainable pattern of growth, focused on high-value exports, private capital ventures, and service industries.¹



Reflective of this new trend is the introduction by Chinese President Xi Jinping of a government-wide policy of the “new normal,” as unveiled by President Xi at an APEC meeting in Beijing in early November 2014. This new policy focuses less on the rapid, and highly impressive, double-digit growth rates China experienced in the 1990s and early to mid-2000s, bolstered by “smokestack” industries and massive infrastructure investment, and more so on lower and more stable rates of growth led by a restructuring of state-owned enterprises (SOEs) and emphasis on consumption, especially domestic consumption. In the light of yuan devaluation and the wild downward swings of China's stock market in 2015, the Chinese government has actively intervened in the stock market and has also delayed market reforms it had planned to implement, worrying some reform-minded investors.

¹ OECD, China – Economic forecast summary, June 2015; KPMG, China Outlook 2015; United Nations, World Economic Situation and Prospects 2015.

Fears of a full-scale “Chinese market melt down,” however, have now been acknowledged as overblown, as the Chinese economy looks to remain on track for continued 6.5–7%-plus GDP growth over the next decade. China also still remains poised to overtake the United States in real GDP output over the next five to ten years, having already surpassed the United States in terms of GDP purchasing power parity (PPP) in 2014.

1.2 Produce Market Overview

China is by far the largest producer of vegetables in the world, accounting for over 50% of the total global production; the agricultural sector comprises approximately 13% of China’s total GDP. In 2013, China’s production value of fresh vegetables surpassed \$25.25 billion, dwarfing the second-largest producer, India, at \$6.25 billion. Similarly, China is also the world’s largest fruit producer, accounting for roughly 20% of total world fruit production with production rapidly rising from 126 million tons in 2000 to 260 million tons in 2014; preliminary reports for 2015 indicate that this trend has indeed continued.

A unique characteristic of China’s fruit and vegetable production system is that produce is almost entirely consumed domestically, quite unlike most other countries’ systems of fresh produce production. In 2014, Chinese exports of vegetables were valued at \$8.23 billion, 12.3% of global vegetable production; Chinese fruit exports were substantially lower, totaling \$4.32 billion in 2014, only 4.1% of global fruit exports.² Nevertheless, due to the sheer production volume, China is now an important importer and exporter of fresh fruit and vegetables. Advances made in production, post-harvest handling, processing, and logistical technologies, and increased levels of international investment, have contributed to the rapid increase in production capabilities and the success of China’s overall produce export market, especially among exports of vegetables. China’s rapidly increasing fresh fruit and vegetable production and imports are driven by steady economic growth that led to a rise in overall household income in China. Consumption levels associated with the rise of this new middle class sparked greater consumer interest in variety, freshness, convenience, and year-round availability of fresh produce.

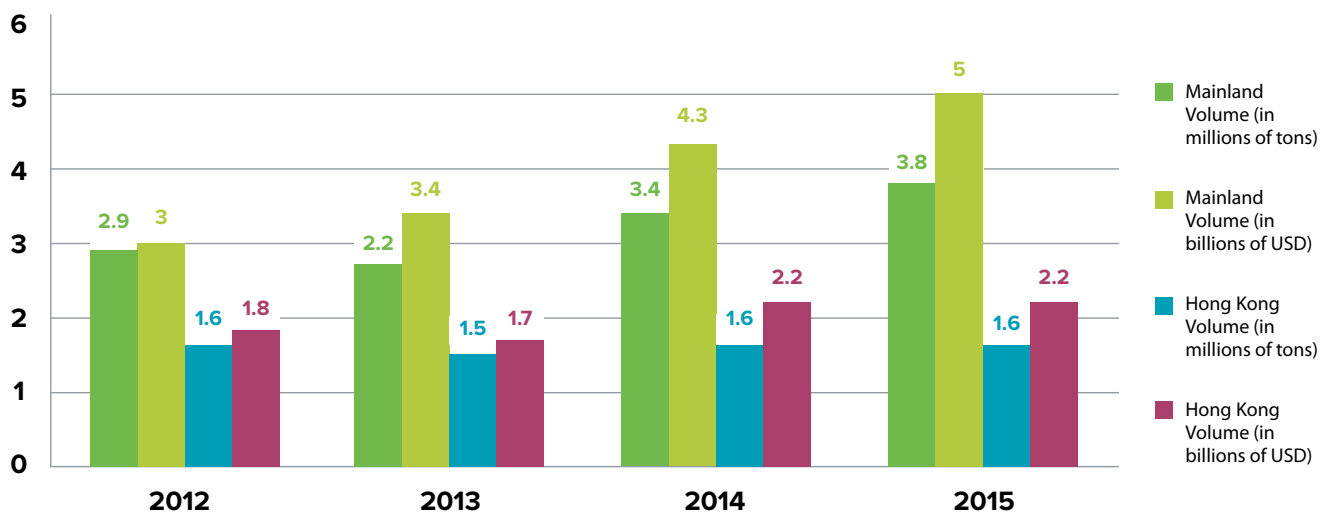
1.3 Imported Fruit Market Overview

China’s imported fruit market witnessed steady growth, both in terms of total import volume as well as import value in the past several years. 2014 was exceptional in this regard, as the total volume of imported fruit to mainland China increased by 27% over 2013, with total value of imports also rising 21%. This trend continued into 2015, with the total volume of fruit imports to mainland China growing to 3.8 million tons and valued at \$5 billion (year-on-year increases of 10.5% and 14%, respectively). Despite a large increase in overall value in 2014 (22.7%), fresh fruit imports to Hong Kong experienced

² International Trade Centre, 2014

very little growth in 2015, as foreign exporters turn from export to Hong Kong to direct export into mainland China as their primary method of distribution—an indicator of the increased difficulty of exporting via grey channels:

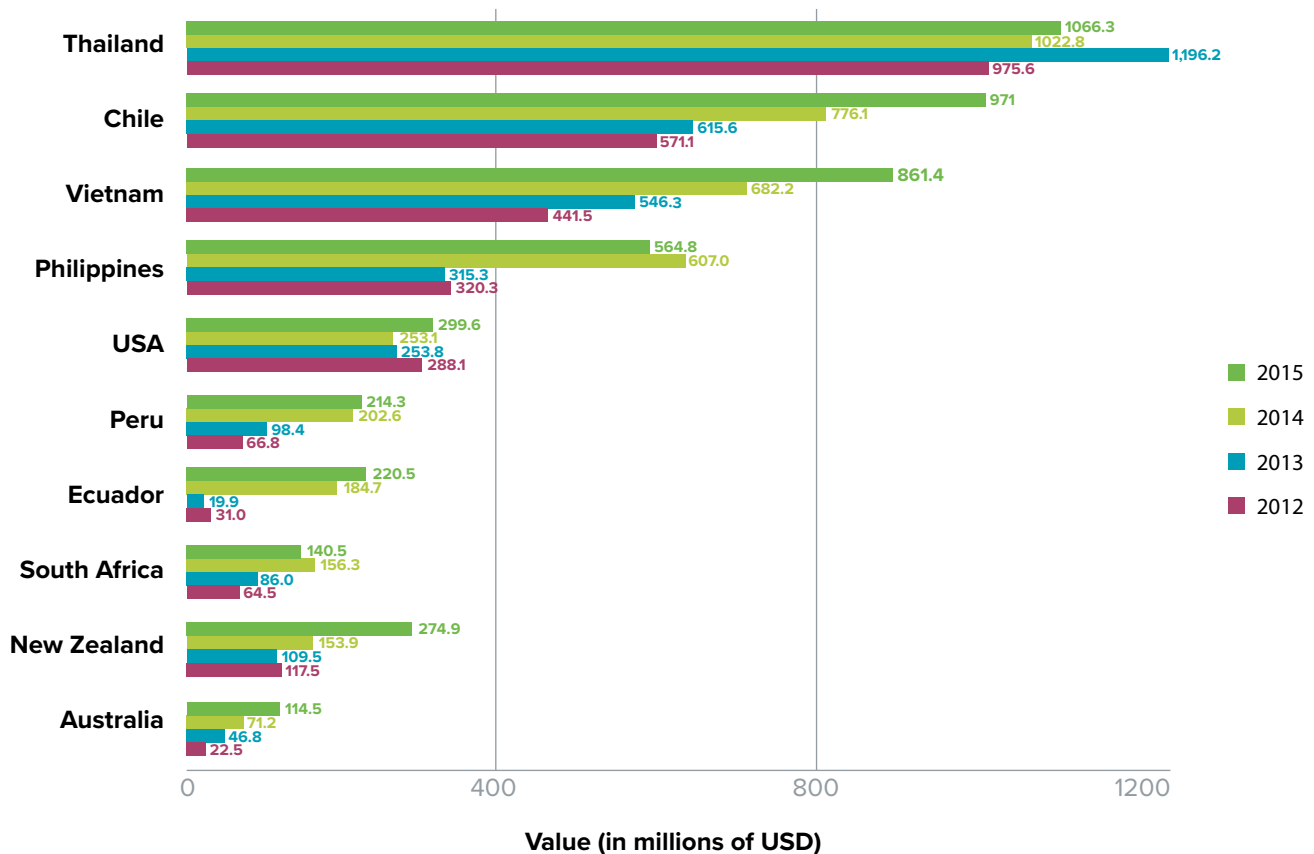
Figure 1:
Total Fresh Fruit Import Value and Volume for Mainland China and Hong Kong, 2012–2015



Source: China Customs, HK Customs

In 2015, Thailand remained the sole country to exceed \$1 billion in total export value to mainland China, even despite a decline in overall value of 12.1% as compared to 2013 levels. Both 2014 and 2015 saw rapid growth in total fresh fruit import value in mainland China. Ecuador witnessed explosive growth as the value of its banana exports to China rocketed from less than \$20 million in 2013 to nearly \$185 million in 2014, an increase of 828%. The Philippines also saw a nearly 100% growth rate in exports to China, but faltered in 2015. This was repeated by both South African and Peruvian fruit exports, which nearly or more than doubled in 2014 but experienced significantly slowed and even negative growth in 2015. Fruit exports from Chile, Vietnam, New Zealand, and Australia were the major success stories of 2015, as exports from New Zealand grew by nearly 80%, Vietnamese by 26%, and Chilean exports nearly matched those from Thailand, rocketing to \$971 million in total value.

Figure 2:
Total Fresh Fruit Import Value for Mainland China by Country, 2012–2015

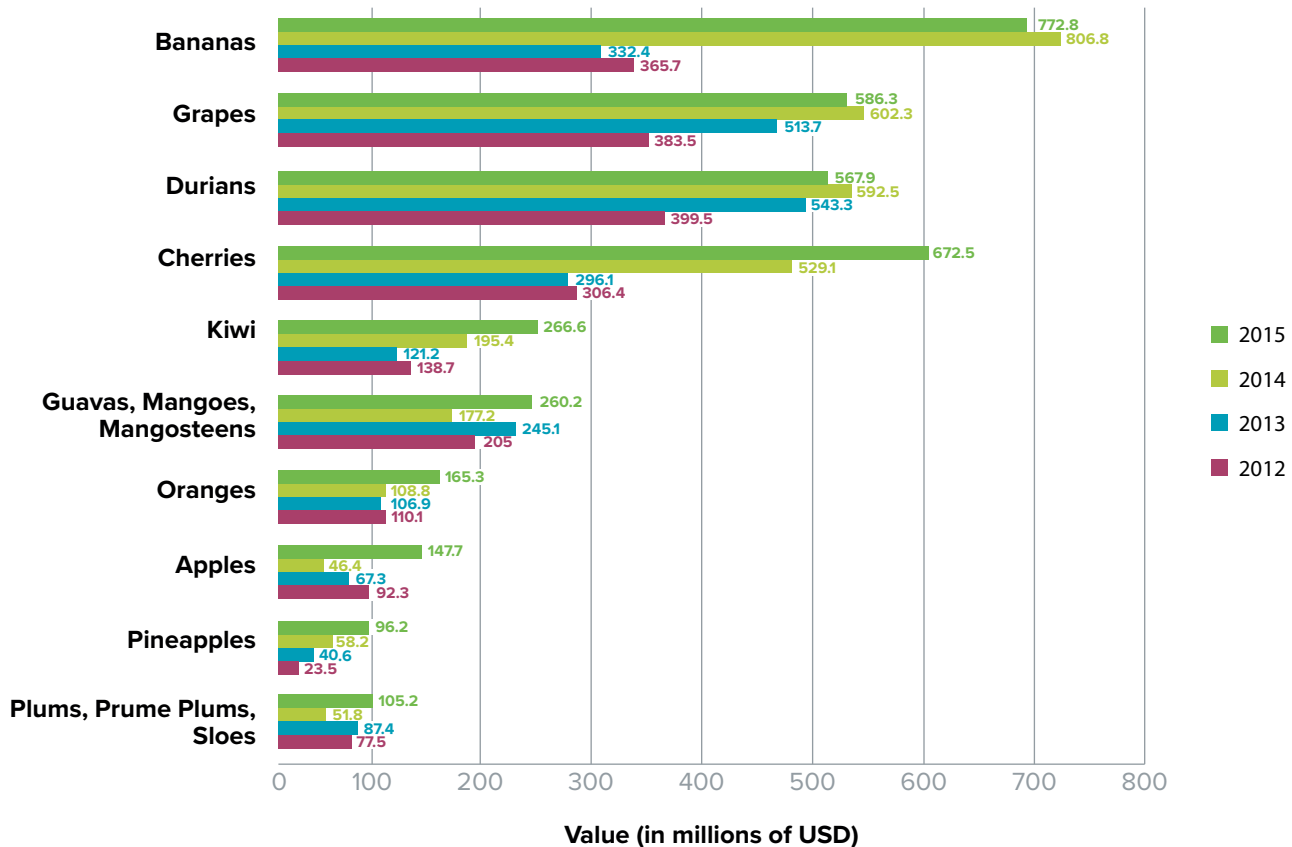


As seen in Figure 3, bananas experienced a breakout year in 2014, with overall imports up by 142.7%, driven by extremely strong export growth from the Philippines (\$555.1 million, a 100.4% increase over 2013) and Ecuador (\$185.7 million, an 824.9% increase). 2015 saw decreases in import value of the top three out of four fresh fruit categories, with bananas, durians, and grapes all slightly declining in value. However, these were the only categories out of the top ten which declined in 2015, as 2015 in general was a big-bounce back year for several categories of imported fresh fruit, most notably guavas, mangoes, and mangosteens (-27.7% in 2014, +46.8% in 2015); plums, prune plums, and sloes (-40.7% in 2014, +103% in 2015); and apples, which rebounded from \$46.4 million in 2014 to \$146.7 million in 2015, an increase of over 215%—in large part due to an easing of varietal and geographic restrictions on apples from the United States.

The rapid and seemingly sustained growth of the cherry in China continued to be a major success story of 2015, as strong growth in cherry imports in 2014 carried over into 2015, with a two-year growth rate

of 127.1% over 2013. This was driven by strong export growth from both Chile and the United States. More than 300,000 5kg boxes of cherries from Washington state alone were exported to China in 2014, a 100% increase over the previous year.

Figure 3: Total Fresh Fruit Imports for Mainland China by variety, 2012–2015



Outside of the top 10 fruits exported to China, listed in Figure 3 above, some other fruit varieties experienced rapid growth in the past several years. Avocados from Mexico achieved a growth rate of more than 400% in 2014 (and have managed to maintain this growth rate since 2011). Categories showing great future potential in 2015 include the import growth of berries into China, such as blueberries, raspberries, blackberries, mulberries, and loganberries.



2. Chinese Governing Bodies Overseeing Imports

2.1 AQSIQ

The General Administration of Quality Supervision, Inspection and Quarantine of the People's Republic of China (AQSIQ) is, as it claims, a “ministerial administrative organ directly under the State Council of the People's Republic of China in charge of national quality, metrology, entry-exit commodity inspection, entry-exit health quarantine, entry-exit animal and plant quarantine, import-export food safety, certification and accreditation, standardization, as well as administrative law-enforcement.” As of October 1, 2015, interested foreign food exporters to China must register under the new AQSIQ registration system (<http://www.aqsiq.net/importer-register.htm>) and fill out the Food Exporter application, whereupon the AQSIQ will grant the exporter an AQSIQ registration number. When assessing and determining the viability of a product's market access, AQSIQ operates according to the following criteria:

- All countries are given the equal opportunity to apply for market access, with an internal minimum of one case per country being processed at any time
- Preference and expedience are given to those categories and varieties of fruits with low pest-carrying risk
- The applicant's product must be in compliance with existing AQSIQ requirements governing same or similar products from other regions and areas
- The exported product must be in accordance with International Standards for Phytosanitary Measures (ISPMs) in order to conduct Pest Risk Assessment (PRA) and Pest Risk Management (PRM)
- The ability of AQSIQ to employ its limited labor resources in processing applications based on the relative complexity of each export application

2.2 CIQ

Directly under the administration of the AQSIQ is China Inspection and Quarantine (CIQ), which was merged with the State Bureau of Quality and Technical Supervision in 2001 to form the AQSIQ. CIQ operates under the mandate of the AQSIQ and retains roughly 35 offices across China, sometimes referred to as Entry-Exit Inspection and Quarantine Bureaus, which serve several key functions:

- Maintain a clear line of communications with laboratories and local offices to ensure import quality standards are upheld
- Function as entry/exit-port inspection agents with the power to seize goods from foreign exporters due to missing or incorrect certifications or documentation
- Ensure that CIQ labels are attached to certain categories of imported goods before entry into the Chinese market

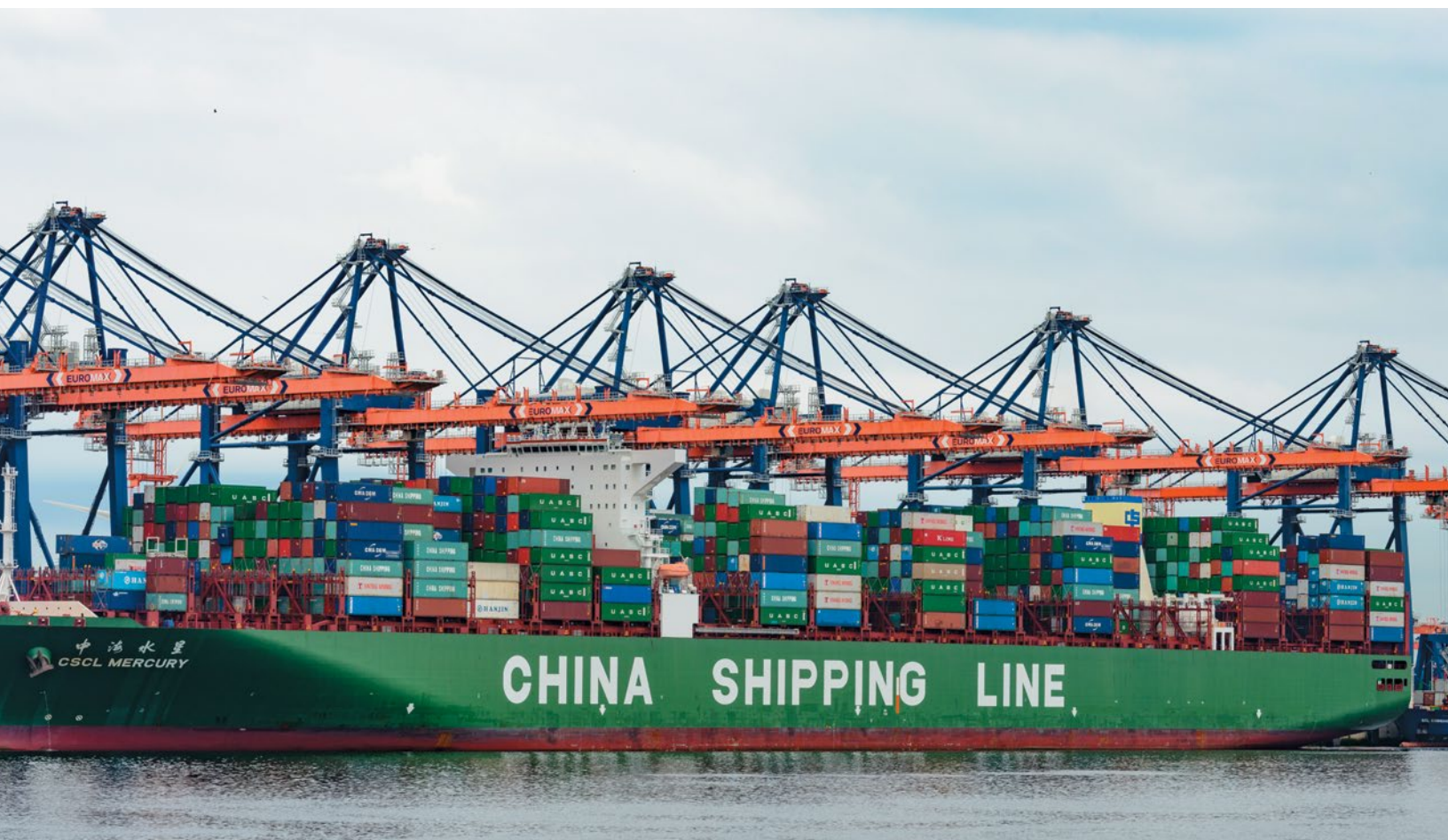
2.3 CIQA

The China Entry-Exit Inspection and Quarantine Association (CIQA) is a non-profit governmental societal organization under China's Ministry of Civil Affairs and AQSIQ, comprised of Chinese enterprises, institutions, societies, and individuals who operate on a volunteer basis. CIQA functions as a bridge between government and business/civil society in the sphere of entry/exit quarantine and inspection, filling regulatory gaps as needed. Often operating on behalf of the AQSIQ overseas, CIQA also works bilaterally with foreign agencies in developing frameworks for coordination and cooperation. To this end, CIQA sponsors technical workshops, seminars, and presentations on increasing cross-sector cooperation, and has the authority to sign a Memorandum of Understanding (MoU) with bilateral partners to facilitate mutually beneficial engagement on issues of imports, exports, and international trade.

2.4 GACC

For all import/export products over which it has regulatory power, AQSIQ maintains the greatest level of importance (and power) in the process of achieving market access in China. Nevertheless, the General Administrations of Customs of the People's Republic of China (GACC) still plays a crucial part in the import and export of products into and out of China after the AQSIQ inspection and quarantine process has finished and product application has been approved. GACC is the headquarters of China Customs and reports directly to China's State Council. General practice requires that the Chinese importer collects and submits the following documentation to China Customs: the bill of lading, invoice, shipping list, customs declaration, insurance policy, purchase and sale contract, and if applicable, the import quota certificate, import license, and/or inspection certificates. The main responsibilities of the GACC in terms of imports and exports are as follows:

- Collection and enforcement of all relevant taxes and duties owed, including value added taxes (VAT), customs duties, tariffs, and various other taxes
- Ensure protection of intellectual property rights (IPR) through the seizure of all suspected counterfeit, smuggled, and patent- and copyright-infringing imports and exports
- Administration and execution of anti-smuggling measures through the use of force by China Customs anti-smuggling police force
- Inspection and verification of all relevant import/export documentation, including examination of discrepancies between the quoted invoice value of goods and actual value
- Compilation, recording, and analysis of trade statistics, including the value, origin, destination, trade, and transport method of import and export goods



3. Market Entry Strategies for Import into China

3.1 Overview

Numerous market entry strategies exist for foreign fruit and vegetable exporters looking to gain access to Chinese markets. The most suitable method of entry is dependent on numerous factors, such as the permissibility of the exporter's fruit and vegetable product to be imported into China, which distribution channels the exporter plans to operate, and the exporter's choice of Chinese importing partner.

It is advised that exporting parties contact their respective government departments and officials (country embassies), hire a consulting company or law firm for intellectual property concerns, or seek other such external advice in addition to conducting their own research before settling on an entry method.

3.2 Pre-Market Access Procedures

The first—and most important—step in obtaining market access for foreign exporters of fresh produce to China is to determine whether the product and country of origin is included among the list of permitted imported fresh fruit and vegetables into China. As of February 2016, 39 countries have been granted market access to import specific fresh fruit and vegetable categories or items. An official listing of all permissible fruits and countries of origin is maintained by AQSIQ on its website, which is only available in Chinese. The latest list can be accessed in English at the following link: <http://bit.ly/1NkxaCo>.³

If both the intended fruit and vegetable export item and country of origin are listed, then technical market access has been achieved and the exporter can begin to explore their options concerning distribution channels and importers/import partners. If either the country of origin or specific fruit product are not listed by the AQSIQ as allowed import into China, technical market access has not been achieved and the exporter must initiate bilateral discussions between their own government and Chinese officials.

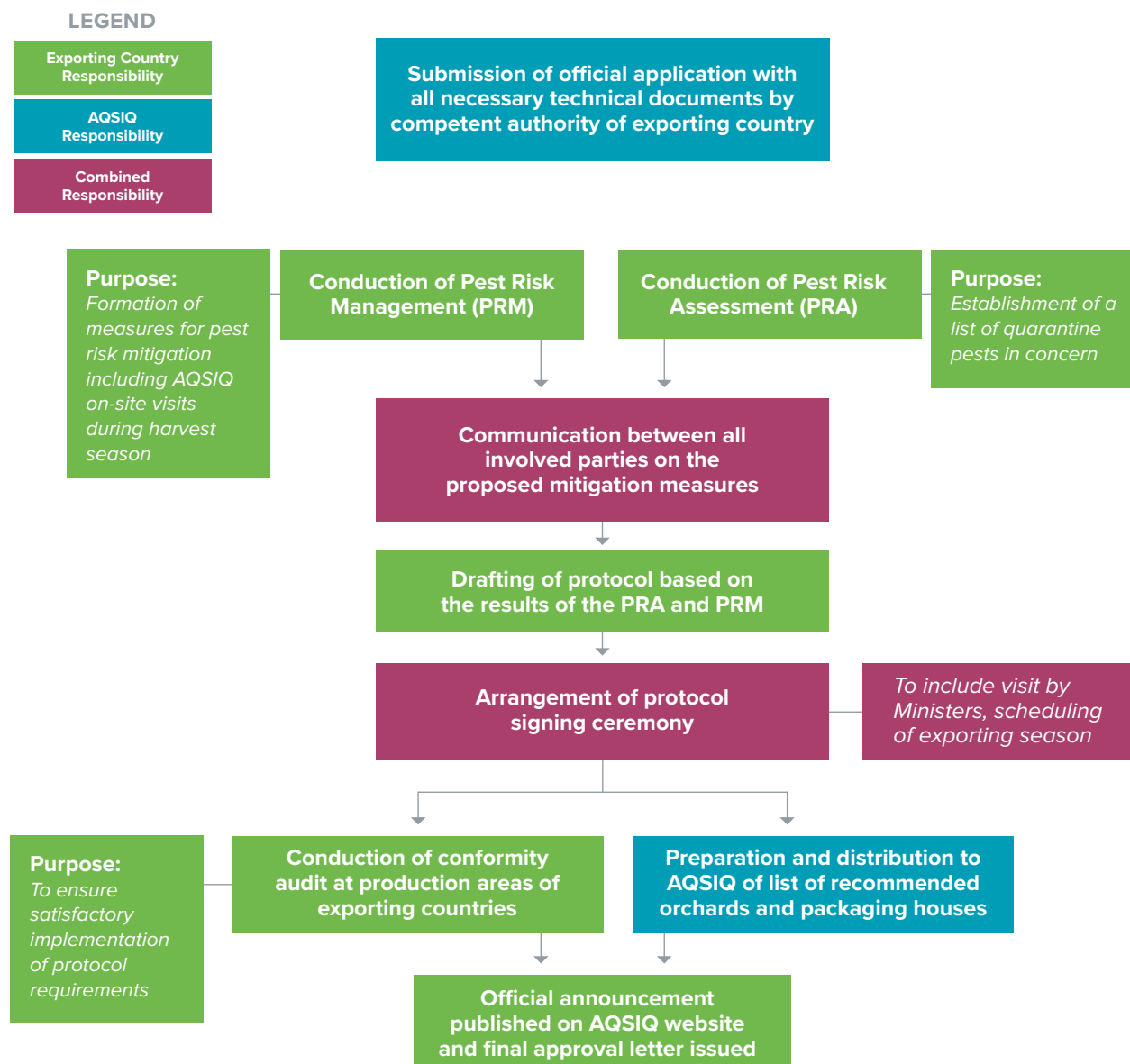
3.2.1 Achieving Technical Market Access

On issues concerning achieving technical market access, foreign exporters must operate through their own countries' embassies in China, most often their agricultural sections, in order to initiate a market access dialogue with AQSIQ. Cooperation with industry associations or groups can be highly advantageous in stimulating bilateral negotiations between the exporter's own government and Chinese officials. Exporters can operate through these industry associations and groups to work with their corresponding national agricultural department, given that such associations or groups exist in the exporter's own country for the fresh fruit product they intend to export to China.

³ AQSIQ: Latest List of Allowable Imported Fruits (Feb. 6, 2016); February 22, 2016.

For Chinese import authorities, the biggest technical concern in granting market access is pest/disease control and quarantine procedures, with protection of China’s domestic produce industry as the primary objective. Fruit imports from countries with a high risk of or ongoing pest problems, such as an outbreak of Mediterranean fruit flies, will have a much tougher and slower time gaining market access in China than lower-risk fruit imports. Obtaining technical market access for a fresh fruit product relies on adherence to specific criteria stipulated by the AQSIQ and constant communication between involved parties, as shown in Fig. 4 below:

Figure 4:
AQSIQ Fresh Fruit Market Access Procedure



Exporters can help expedite the status of their applications by ensuring that all information submitted to the AQSIQ is both comprehensive and promptly submitted, and that they quickly respond to any further inquiries by the AQSIQ. Constant effort must be expended by both the government and industry groups of the exporter's country to ensure that communication is open and a close working relationship is maintained with the AQSIQ and other Chinese import officials. This can be assisted through the establishment of cooperative mechanisms, conferences, meetings, or other such events bilaterally between both sides at the governmental and trade/industry level.

3.2.2 Political Factors

Market access for fresh fruit and vegetable imports into China is both a technical and a political issue. Maintaining good bilateral relations is important in gaining expeditious market access, and is a difficult issue to remedy for exporters whose countries have a less-than-satisfactory relationship with the Chinese government. Exporters whose countries have signed a Free Trade Agreement (FTA) with China enjoy a large competitive advantage in the form of tariff waivers;⁴ the majority of these countries have tariff-exempt regimes or are progressing toward a tariff-less state for fruit imports, with the only imposed tax being a 13% VAT. Eight countries in Southeast Asia, most notably Thailand and Vietnam, are exempt from import tariffs on their fruit exports to China, with Chile and Peru in South America also enjoying tariff-free fruit exports to China. The rate of tariff reduction varies from country to country and is based on both political and technical factors. Tariffs on Australian fruit imports are expected to be lowered to 0% over a five-year period, whereas Korea's only permitted fruit export to China, table grapes, will take up to ten years for a state of zero tariffs to be achieved. Exporters whose countries have not signed FTAs with China are far less competitive and face significant pricing challenges in the Chinese imported fruit market compared with exporters looking to expand into the Chinese market with the benefit of having an FTA already in place.

Reciprocal market access, especially for apples, pears, and citrus, is sometimes sought by Chinese authorities as a condition for allowing fruit imports from a certain country into China. This issue is often out of the control of the exporter and can present a roadblock in negotiations, to either be resolved at a higher executive level or after certain concessions have been made.

Exporters can look to Chile's success in the Chinese imported fruit market as a model worthy to follow. Chile has enjoyed strong bilateral economic relations with China following the signing of an FTA with China in 2006, which led to a surge in the number of permissible fruit categories for export to China and quicker AQSIQ application processing times. Combined with efforts by the Chilean government and fruit industry to increase Chinese consumer awareness of Chilean brands and hosting "Made in Chile" public relations campaigns (such as the "Week of Chile in China" in August 2015), Chile has grown to become the largest fresh fruit exporter in South America to China.

⁴ See Appendix A for full list

3.3 Selling to Importers, Retailers, and E-Commerce

In order to navigate China’s complex set of import rules and regulations and complicated supply chains, establishing networks and working through Chinese distribution and import partners are necessities for almost all foreign exporters looking to expand their business into China, especially smaller firms with little previous experience and networks in China. Potential Chinese import partners can include one or more of the following:

IMPORTERS

- Possess networks and relationships with distributors and China’s governing import bodies to navigate China’s complex system of distribution
 - Can operate both as a wholesaler and a distributor to retailers
- Handle China Customs’ import processes; manage product stock and inventory
- Offer services to a large number of foreign exporters
 - Import agents can also operate as exclusive partners for specific foreign exporters

RETAILERS

- Include supermarkets and hypermarkets such as CRV, Walmart, Carrefour, etc.
 - Retain advanced distribution networks and established cold chain infrastructure throughout Tier I and Tier II cities
 - Work with foreign exporters on in-store branding and marketing efforts
- Fresh fruit “boutique” chain stores (e.g. Pagoda)
 - Emphasis on close collaboration with suppliers/importers and direct import of foreign and domestic high-end, high-quality produce
- Provide “online-to-offline” (O2O) services (purchase online, physical pickup)
- Direct import sourcing removes need for “middleman” importing agents

E-COMMERCE WEBSITES AND COMPANIES

- Smaller import volumes, generally source via distributors or direct importing
 - Yiguo and FruitDay—largest fresh fruit e-commerce platforms
- Operate primarily in Tier I markets with well-established cold chain infrastructure and more affluent consumers with specific preferences in fresh fruit
- Provide end-to-end, 1–3 day complete order-to-delivery consumer services
- Function independent of distributors, wholesale markets, and retailers
- Able to quickly react to market fluctuations and imported fruit surpluses/shortfalls

3.4 Representative Office

Establishing a representative office (RO) in China is an effective and quick way to enter the Chinese market for certain businesses. ROs require minimal overhead investment and provide their parent company with the opportunity to conduct market research independent of Chinese importers and other partners; form networks and establish business contacts with distributors, retailers, and other clients on behalf of the parent company; coordinate parent company's activities in China; and engage in quality control. ROs can also operate as a marketing agent and brand-builder for foreign exporters in China. In April of 2015, six New Zealand companies from various agricultural sectors joined forces to open a new company and RO in Shanghai, the Primary Collaboration New Zealand Company Limited (PCNZ), whose primary objectives were to promote market awareness and brand consciousness among Chinese consumers as to New Zealand and made-in-New Zealand products and exports.

As a tool in the fresh fruit import supply chain, an RO's function can be relatively limited, as foreign ROs in China cannot engage in profit-making activities, are forbidden from signing contracts on behalf of the parent company, and cannot possess more than four employees. Most foreign fresh produce exporters would have minimal use for a China-based RO, but for larger fresh produce exporters or groups and associations of exporters seeking to expand their presence directly in China, establishing an RO in China can prove the first step in further, more expansive development.

3.5 Wholly Foreign-Owned Enterprise (WFOE)

A wholly foreign-owned enterprise (WFOE) is the most common form of foreign investment in China. WFOEs can import directly from their home country without the need to go through a third party while possessing their own quality control and assurance mechanisms. The foreign exporter retains complete control over the company with no Chinese partner involved, and is permitted to distribute its products throughout China. The exporter is itself responsible for all Chinese operations, maintaining local networks and connections, and navigating the difficulties of customs processes all in Chinese. Previously, the initial prohibitive setup cost, time-consuming and complex application processes, and overall difficulties of operating in China without a Chinese import partner were the largest factors in limiting the number of WFOEs in the foreign produce export sector. However, recent improvements in bureaucratic processes and overall ease of application have made it much easier for WFOEs to establish themselves in China, especially if the company is set up to operate in China's Free Trade Zones (FTZs), most notably the Shanghai FTZ.

3.6 Joint Venture

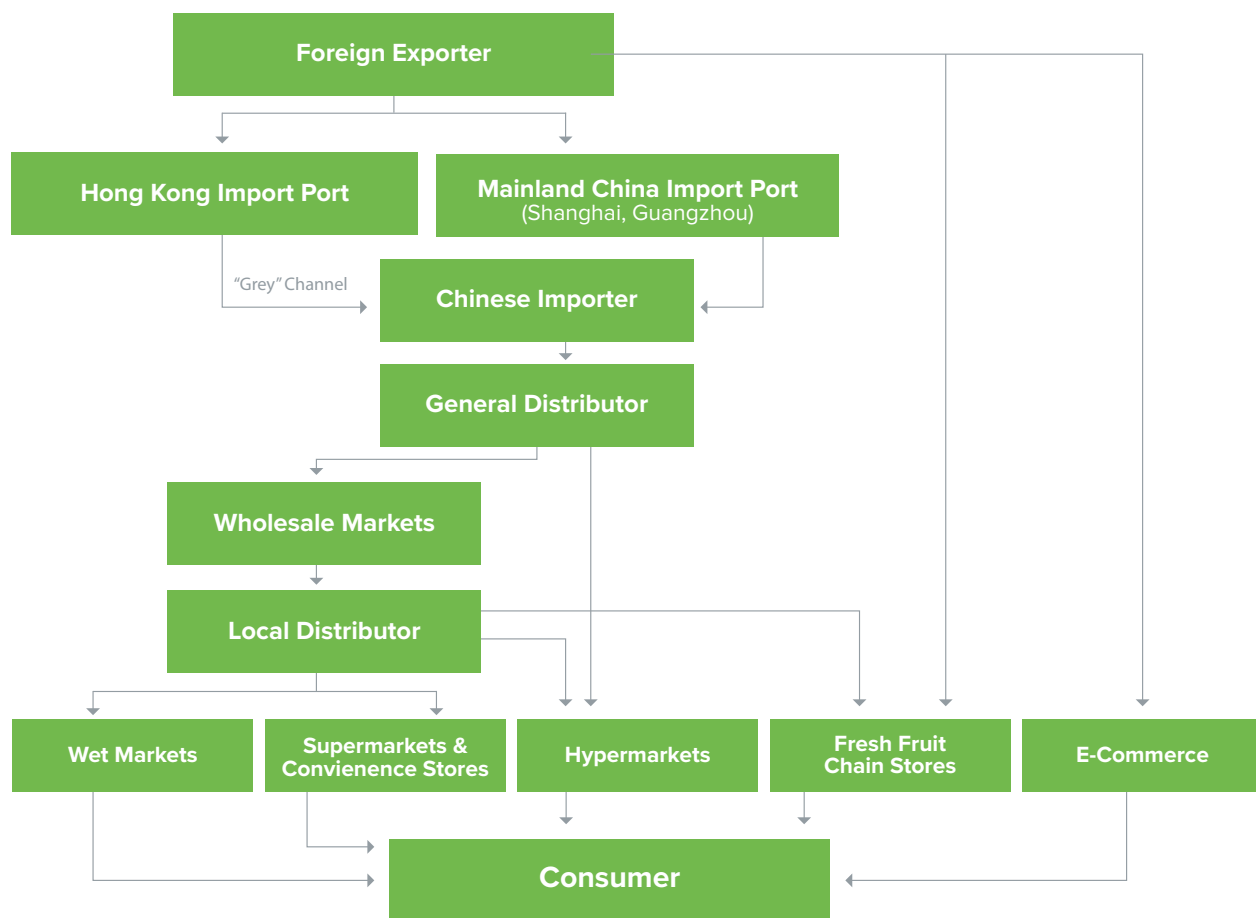
The major advantages of operating as a joint venture in China is the ability for the foreign exporter to utilize their Chinese partners' distribution and sales channels, workforce, facilities, and relationships and networks with government officials to avoid unnecessary bureaucratic red tape and delays. However, this comes with its own drawbacks, as the exporter is highly reliant on the Chinese partner and shoulders the cost and risk associated with potential differences in management styles, business interests, and profit sharing between companies.

Fresh produce export joint ventures in China are extremely rare. When they are formed, they are for cases where a foreign entity wishes to set up domestic Chinese production facilities to supply domestic consumption. In 2008, Chiquita Brands International entered into a JV with Chinese processor Haitong Food Group Co. with the intent to enter into the Chinese value-added produce market. Chiquita provided capital investment and its expertise in fresh produce logistics, marketing, distribution, and food safety, whereas Haitong was involved in the food processing operations in Cixi, China, and the marketing and sale of value-added produce, such as fresh-cut fruits and vegetables, packaged salads, and fresh chilled beverages throughout China. For the vast majority of foreign fresh fruit exporters, JVs are unnecessary when expanding into the Chinese market.

4. Distribution Channels

4.1 Overview

Figure 5: China's Imported Fresh Produce Distribution Model



Source: EU SME Centre Sector Report: The Food & Beverage Market in China 2015; USDA 2014 Retail Report

Traditionally, imports of foreign fresh fruit and vegetables into China have followed the distribution model of import into Hong Kong, followed by transit into mainland China via legal, illegal, and “grey” distribution channels and transportation to major wholesale markets along the coast of China, whereupon distribution to wet markets, supermarkets, and other wholesale markets in China’s interior occurs. This distribution model is characterized by numerous aggregators, vendors, and distributors, sapping profits from the exporter and reducing value for the consumer. However, this model has evolved, and the present imported fresh fruit supply chain model in China is currently moving away from third-party aggregators, agents, and distributors and is moving toward more direct distribution models, such as direct import to mainland China from foreign exporters and e-commerce.

4.2 Distribution Channels for Foreign Exporters into Mainland China

The two most common methods for exporters of fresh fruit to gain access to the Chinese market are exporting to mainland China via Hong Kong or direct export to mainland China. Depending on the distribution channel chosen, the foreign exporter’s China partners will vary. However, it is highly advisable for newer, smaller exporters to initially operate through reputable, carefully chosen Chinese importers, regardless of distribution channel and method.

4.2.1 Exporting via Hong Kong through Grey Channels

Foreign fresh fruit and vegetable exporters have long utilized Hong Kong as a conduit to the markets of mainland China. Hong Kong operates as a free port, and as such enjoys zero tariffs, VATs, and other duties, guaranteed by the Sino-British Joint Declaration until at least 2047. Fresh fruit exports utilizing this channel are first imported to Hong Kong and then reimported into mainland China, more often than not through “grey” channels. A grey channel refers to partially legal/partially illegal⁵ distribution channels where imported goods avoid partial or full tariffs and duties as well as partial or non-compliance with phytosanitary and quarantine requirements, facilitated through the provision of false or manipulated documents.⁶ Importers who utilize grey channels cite advantages such as timely market access for perishable and spoilable export products, evasion of tariffs, duties, VAT and other taxes, avoidance of rigorous and lengthy Chinese quarantine and inspection procedures, and gaining market access for categories of fruit from certain countries which have not yet been granted market access to the Chinese market by AQSIQ.

However, the risks associated with the grey channel in China have continued to grow over the past decade, with crackdowns by Chinese authorities on imports using grey channels becoming more frequent and more severe. Stimulated both by attempts by the central government to recover revenue lost from tariffs and duties as well as a more widespread anti-corruption drive initiated by Xi Jinping following the 18th National Congress in November 2012, the legal ramifications of using grey channels to import products into China have greatly increased, with harsher fines and longer imprisonment sentences facing grey channel importers caught evading duties and quarantine requirements.

⁵ Often referred to as “semi-legal.”

⁶ Ray Collins and Ximing Sun, “China’s grey channels as access points for foreign food products to the Chinese domestic market,” *China Information*, Vol. 24, No. 1, March 2010, 62-63.

Additionally, complete product loss can result from grey channel activity, either through the confiscation of suspected goods by Chinese customs authorities or through spoilage created by inspection backlogs for suspected goods entering China at the China-Hong Kong border. Grey channel fresh fruit imports also run the risk of identification by customs authorities, which could result in country of origin import bans and jeopardize the future of exporters' fruit exports to China. Branding and marketing campaigns cannot be conducted for goods distributed via grey channels, ultimately harming the competitiveness and ultimate success of an exporter's fresh fruit exports to China.

Use of grey channels by importers have dropped in recent years not only due to increased enforcement by Chinese customs authorities, but also because of China's import tariffs and duties becoming lower as a result of China's gradual implementation of WTO standards on imports, with tariffs even being fully waived for countries who have signed FTAs with China. Therefore, it is highly advisable for foreign exporters to avoid using grey channels in accessing the markets of mainland China.

4.2.2 Direct Export to Mainland China

Direct export to China, bypassing Hong Kong and various grey channels, has become the premier distribution method for foreign exporters of fresh fruit and vegetables to China. Exporting directly to ports in mainland China, namely Guangzhou and Shanghai, is the most efficient market access method, as the added complications of transport and cold storage through Hong Kong are eliminated. Furthermore, Chinese authorities have established Free Trade Zones (FTZs) in Shanghai (2013), Tianjin, Guangdong, and Fujian (2015). These ports enjoy integrated quarantine and inspection, with a turnaround time ranging from 48 hours to 6 hours (Shanghai's Yangshan bonded area), not only cutting costs for importers but also preserving product freshness and ensuring swift delivery to customers. Shanghai remains the preferred entry port for fruit exports to China, as other major ports such as Beijing suffer from longer and less convenient shipping routes and lengthier quarantine procedures.

Additionally, cold chain infrastructure and transportation has increased exponentially in China, growing from a cold storage capacity of 10 million m³ and 12,000 refrigerated vehicles in 2007 to a capacity of 106 million m³ and 89,000 vehicles in 2015.⁷ This rapid growth in cold chain infrastructure is concentrated in major import ports and FTZs such as Shanghai, Guangzhou, Fujian, and Tianjin, reducing Hong Kong's importance as port of entry for foreign fruit imports. With the rise of e-commerce in the Chinese imported fresh fruit market, risks previously associated with payment and credit, such as unreliability of payment from Chinese consumers and importers, and delays in full payments being received, have been lessened through reputable online payment methods directly connected to fresh fruit e-commerce websites. For efficiency, spoilage prevention, lower costs, and general ease of access, fresh fruit exporters are recommended to utilize direct export as their primary distribution channel to mainland China.

⁷ 'From Freight Trains to Cold Chains,' Rabobank FAR, November 2015.

4.3 Wholesale Markets

There exist over 4,000 wholesale markets across China, with each city typically hosting several major wholesale markets. Beijing's Xinfadi Agricultural Market is the largest wholesale market in northern China, and is the source for 70% of all vegetables and 80% of all fruit consumed in Beijing. Guangzhou's Jiangnan Wholesale Fruit and Vegetable Market is the most important imported produce wholesale market in China, accounting for 70% of all imported fruit and vegetables into China. A Jiangnan expansion wholesale market, Huizhan Fruit & Vegetable Wholesale Market, which enjoys streamlined customs controls and specific quarantine inspection stations, was established in August of 2013 in Shanghai as well, cementing Shanghai as a main port for imports of foreign fruits into China. Upon leaving the wholesale markets of Guangzhou, Shanghai, or Beijing, imported foreign fruits enter into a highly fragmented cold supply chain on its journey to Tier II and III cities. Cold chain infrastructure is severely lacking in these cities and is one of the major challenges facing expansion of foreign fresh fruit imports into the wholesale markets of Tier II and III cities.



4.4 Retailer Sector and Market Potential

China's retail market is forecast to be valued at over \$1.5 trillion by 2016, an increase of 68% since 2012. Supermarkets and hypermarkets in China have witnessed generally consistent growth over the past decade; in 2003, their share of all retail sales comprised 30% of the market, rising to 50% by 2014 at the expense of wet markets, independent shops, and individual convenience stores. (However, wet markets remain the preferred sales channel for imported and domestic fresh fruit among many Chinese consumers.) China's largest retailers are primarily regional as opposed to national, with some retailers possessing a market share as large as 30% in individual provinces.⁸ However, since 2013, supermarket and hypermarket growth rates have experienced a significant slowdown, a result of online competition and e-commerce, increasing operation and overhead costs, and growing ambivalence among consumers toward supermarkets as their main shopping destinations.

China's retail sector is comprised of both domestic and foreign players, with the largest retailers being C.R. Vanguard (domestic), R.T. Mart, and Walmart (both foreign). Foreign retailers continue to enjoy a strong reputation amongst Chinese customers as sources of high-quality, fresh, and ingredient-safe imported produce. However, foreign retailers such as Carrefour and Metro Cash and Carry have seen

⁸ Agriculture and Agri-Food Canada. Consumer and Retail Trends in China, March 2014.

sales fall in the past five years as domestic retailers continue to improve their reputation in terms of food safety and quality, as well as increasing offerings of imported goods and produce. Walmart itself was forced to close 16 stores in 2014 and the retailer's overall sales in China fell by 6% in that same year; nonetheless, Walmart has since announced plans to increase its presence in China by roughly one-third through the opening of 115 new Walmart outlets in China by 2017. Both domestic and foreign retailers still present lucrative opportunities for fresh fruit exporters, as in-store promotions of imported fruit remain popular among consumers and cooperation with retail outlets still effective in increasing consumer awareness and in-brand promotion.

4.4.1 Emerging Trends in Retail

The growth of premium supermarkets and hypermarkets, featuring high-quality imported produce and catering to middle-and upper-class consumers, has slowed in 2014 and 2015, with competition numerous and fierce, and high market saturation in Tier I cities. However, some retailers are adapting to market trends with new sales methods, such as specialized fresh fruit boutiques, markets in FTZ areas, and O2O e-commerce⁹, and are thriving as a result.

4.4.2 Fresh Fruit Boutique and Chain Stores

Fresh fruit boutique and chain stores are becoming another force to be reckoned with in both the imported and domestic market for high-quality fresh fruit. These specialty stores sell primarily high-end, high-quality produce both online and offline to middle and upper class consumers. Strict adherence to advanced standards of cold chain management and transportation ensures that the quality and freshness of imported fruit produce is preserved, facilitated through close partnership with distributors and suppliers. At the forefront of this emerging market is Pagoda, China's first and most successful specialized fruit shop chain and recipient of Asiafruit Congress's "2015 Produce Retailer of the Year." Pagoda set up shop in 2002 and has enjoyed great success since, opening its 100th store in 2009 and 1000th in June 2015. Over 1,300 Pagoda locations are in operation as of early 2016 across all of China, with plans in place to triple this figure by 2017 and a goal of 10,000 stores within five years. Specialty stores such as Pagoda are attracting a steadily growing base of loyal shoppers not only by their high quality and large variety of fresh imported produce, but also through substantial customer service policies, such as online purchase with free delivery, generous return and refund policies, and friendly and personable store employees.¹⁰ Investment in boutique fruit shops is mounting each year, witnessed by equity/venture capital firm Tiantu Capital's \$62 million Series A financing of Pagoda in September 2015.¹¹

4.4.3 Directly Imported Goods (DIG) Markets

Although current volume is low, a burgeoning prospect for foreign fruit exporters is cooperation with Directly Imported Goods (DIG) markets in China. These consist of premium supermarkets and

⁹ See section 4.5.2

¹⁰ "Pagoda Celebrates 1000th Store Opening with the World's Largest Fruit Plate," Guojiguoshu.com, June 2, 2015.

¹¹ "Pagoda Completes \$62 Million Series A Financing Round," Guojiguoshu.com, September 23, 2015.

hypermarkets located within FTZ areas, and are able to directly import from abroad, benefiting from streamlined quarantine and inspection customs procedures and minimal transportation times and costs. Shanghai's Waigaoqiao DIG imports fresh fruit directly from exporters overseas and has enjoyed enormous success with Shanghai residents.

4.5 Overall E-Commerce Sector

China is the world's largest e-commerce market and is rapidly growing, with online sales surpassing \$670 billion in 2015. One of the main drivers of this exponential growth was sales of online fresh fruit; online purchase of fresh produce is quickly becoming a preferred purchase channel for Chinese consumers, especially among young professionals in Tier I cities. Sales of online fresh produce were nearly \$4 billion in 2014, with industry forecasts predicting a market size of \$16 billion and, total fresh produce market segment of 15% by 2018.¹² Cross-border B2C (business to consumer) e-commerce is quickly establishing itself as a formidable force in the fresh fruit e-commerce landscape, providing consumers with the convenience of ordering fresh imported produce online and it being delivered directly to their doorstep, with end-to-end service times of less than 24 hours and returns offered for up to 48 hours. Quarantine and inspection processes are accelerated for B2C cross-border e-commerce, preserving product freshness, and consumers enjoy tax breaks and tariff and customs duties waivers on small-scale fresh fruit purchases—import duties, tariffs, and the 17% VAT on fresh fruit imports are waived, with a flat 10% customs duty put in place instead. Purchases under 50RMB, or \$8, are subject to no taxes or tariffs at all.

4.5.1 Fresh Fruit E-Commerce Competition

Competition in the imported fresh fruit e-commerce market in China is fierce and primarily domestic, with Alibaba Group and JD.com the two largest e-commerce platforms for imported fruit (and all e-commerce as a whole) in China. Both Alibaba and JD.com have turned to investing in smaller, more specialized fresh produce e-commerce companies to expand their own presence in online fresh produce e-commerce.

JD.com invested \$70 million in FruitDay in May 2015, a high-end fresh fruit retailer founded in 2009. With this, JD.com gained access to China's largest online fresh fruit retailer and its first cross-border fresh fruit e-commerce company (90% of FruitDay's high-quality fruit sales are imported fruit and 50% of these are directly imported by FruitDay). FruitDay began operation in Shanghai FTZ's Yangshan Free Trade Port in 2015, reducing overall costs by 20% and safeguarding product quality and freshness.¹³ FruitDay's sales channels include its official website (www.fruitday.com), mobile apps, online platforms (www.jd.com, www.yhd.com, etc.), and offline channels (shopping channels, O2O stores).

In 2014, Alibaba Group began investing in Yiguo.com (est. 2005), China's first fresh produce e-commerce company. Yiguo is also China's largest vertical fresh produce e-commerce, serving its over three million

¹² USDA Foreign Agricultural Service, "Fresh Fruit Market in North China," GAIN Report # N/A, February 24, 2015.

¹³ FruitDay, The rising China and China Fruit E-commerce, 2014.

loyal and active customers through multiple sales channels, such as via management of Tmall's fresh produce supermarket (chaoshi.tmall.com), Tmall's newly created "Mr. Miao," or "Miaoxiansheng," fresh sales platform (miao.tmall.com), and through sales on their own website (www.yiguo.com) and mobile apps.¹⁴ In March 2016, Alibaba became the world's largest retailer, surpassing Walmart.

By investing in well-established specialized players with loyal customer bases, both Alibaba and JD.com hope to utilize the cold chain management and developed delivery logistics of their partners/ investments to encourage rapid development and growth of fresh produce e-commerce. Other competition is smaller, but numerous and gradually growing, such as Amazon.com, who entered the Chinese fresh produce e-commerce market in May 2014 with its investment of \$20 million in Shanghai-based online retailer and delivery service Yummy77.com. However, without sustained financial backing and access to substantial capital, the future of these smaller fresh produce e-commerce ventures can be volatile. In April 2016, Yummy77.com filed for bankruptcy, citing liquidity problems caused by disputes among investors.¹⁵

4.5.2 O2O E-Commerce

Online-to-offline (O2O) commerce represents a growing opportunity for both China's e-commerce companies and retailers alike. Consumers have been drawn to the convenience of shopping for imported goods online and picking up their order at physical, "offline" locations at their own convenience. O2O sales in China have grown 350% since 2011, with sales surpassing \$51 billion in 2015 and expected to double by 2018.¹⁶ There exists large potential for foreign fresh fruit exporters utilizing O2O with Chinese e-commerce companies and retailers as demand for both O2O services and imports of fresh fruit and vegetables continue to increase.

The first half of 2015 witnessed 80% growth in online O2O revenues as compared to the previous year, with Chinese e-commerce companies recognizing this growth and investing accordingly—Alibaba invested \$4.6 billion in retailer Suning Commerce Group in August 2015, and JD.com acquired a 10% stake for \$700 million in domestic supermarket chain Yonghui Superstore, also in August 2015. Following JD.com's capital injection of \$70 million, FruitDay opened 50 new O2O brick-and-mortar stores in Beijing and Shanghai in 2015, together with logistical infrastructure and support from JD.com.¹⁷

However, significant challenges in ensuring product freshness and quality through O2O channels still remain, such as inadequate or only partial cold storage of produce, high transportation costs, slow and inefficient transportation and distribution networks, and the relative inexperience of some retailers and distributors in the handling of perishable products. As a result, B2C e-commerce generally remains the preferred method of online fresh produce purchase for Chinese consumers.

¹⁴ Eric Li, "China E-Commerce & Fresh Fruit Online," Asia Fruit Market Insight, May 21, 2015.

¹⁵ "Yummy77.com Going Under, Who Will be the Next Casualty in Fresh Produce E-commerce?" Guojiguoshu.com, April 13, 2016.

¹⁶ 2015 China E-commerce & O2O Summary Report, iResearch, January 19, 2016.

¹⁷ M.Z. Marketing Communications, Fresh Produce E-commerce in China, October 2015.

5. China's Population Regions for Distribution

Figure 6: China's Cities

	TIER I	TIER II	TIER III	TIER IV, V, & Rural
# OF CITIES	• 4	• ~30	• ~250-300	• 35,000+
CITIES	• Beijing, Shanghai, Guangzhou, Shenzhen	• Chongqing, Chengdu, Kunming, Hangzhou, Tianjin, Fuzhou, etc.	• Beihai, Guilin, Nantong, Wezhou, Yinchuan, etc.	• Taixing, Changxing, Changshu, Xinmin, etc.
POPULATION & INCOME	• 16 million households • ~\$163 billion household income	• 38 million households • ~\$325 billion household income	• 75 million households • ~\$488 billion household income	• 165 million households • \$~ 1,1138 billion household incomes
CITY CHARACTERISTICS	• Most developed cities, main centers of economic activity in China • Still attract large amounts of foreign and domestic investment	• Provincial/regional capitals or special economic zones (SEZs) • High economic development due to government stimulus	• Prefecture-level cities, population <1 million • Located in coastal areas or satellite cities to Tier I/II cities	• County-level cities and villages in hard-to-reach regions of China's interior • Manufacturing and agricultural-focused
CONSUMER CHARACTERISTICS	• Affluent, sophisticated, cosmopolitan • Preference for imported, high-quality products • Food safety, health foods, organic produce very important	• Rapidly growing middle class with large amounts of disposable income • Growing appetite for foreign fruit imports amidst increasingly high standards for food safety and quality	• Rapidly growing middle class with large amounts of disposable income • Government-promoted economic migration from Tier I cities • High purchasing power due to low living costs	• Price-oriented, preference for domestic over imported fruits • Preference for non-perishable produce
DISTRIBUTION AND COLD CHAIN INFRASTRUCTURE	• Highly advanced and integrated cold chain infrastructure • Rapid end-to-end distribution (24-48 hours), facilitated by FTZs and high e-commerce penetration	• Government and private investment spurring high cold chain sector growth rates • Home delivery offered through third-party logistics providers	• Primarily serviced by long-haul refrigerated trucks • Logistical issues such as underdevelopment and fractured distribution channels exist	• Highly fragmented, broken, and undeveloped • Inconvenient or far from distribution and transport hubs
IMPORTED FRESH FRUIT MARKET: CHARACTERISTICS	• Main entry point for all foreign fruit exports • Location of foreign exporter China-wide product launches • Crucial for foreign exporter to establish base of operations before expansion to other tiers	• Accounts for ~50% of China's total imported fruit consumption • Demand among consumers for foreign fruit imports very high • Increasing frequency of air-freight to deliver foreign fruit imports from Tier I markets	• Supermarkets are hypermarkets main imported fruit purchase locations • Demand continues to rise for foreign fruit imports	• Presence of imported fruit extremely limited • Fruit sales dominated by traditional wet markets • Large potential for future growth, but heavily dependent on continued investment in infrastructure
IMPORTED FRESH FRUIT MARKET: COMPETITION & E-COMMERCE	• Highly competitive, both among domestic and foreign fruit brands • Niche markets, have e-commerce high potential but nearing saturation	• Growing competition amongst foreign exporters as market saturates • Fresh fruit e-commerce growing rapidly	• Low presence of foreign fruit exporters, Chinese brands remain dominant • Fresh fruit e-commerce gaining momentum	• Little to no foreign exporter presence • Competition very low, but ease of doing business also very low

Sources: L.E.K. Consulting, Spotlight on China: Understanding the Chinese Consumer, December 2, 2013;
Nielsen, China 2014 – A New Era in Consumption, April 2014;
International Monetary Fund IMF Working Paper: Understanding Residential Real Estate in China, April 2015

6. Future Opportunities

6.1 China's Growing Middle Class

China's middle class grew to 109 million adults in 2015, surpassing the 92 million adults that comprise the American middle class.¹⁸ Accompanying this growth was a corresponding rise in average consumer spending in China. Between 2008 and 2013, annual consumer expenditure in China increased from \$1,368 to \$2,522, with consumers increasing their spending on fruit products from \$36 to \$71 over the same time period. Euromonitor predicts that by 2018 consumers in China will spend on average \$4,251 every year, with \$113 of that on fruit and fruit products, a 69% increase over 2014.¹⁹ With per capita spending on fresh fruits increasing by 83.7% over the past five years and Chinese middle class consumers projected to spend more than \$650 billion on food products by 2017, numerous opportunities await fresh fruit exporters to China.



6.1.1 Rising Disposable Income

Accompanying the growth of China's middle class is greater disposable income for the average Chinese consumer, which has translated into increased consumer spending. Spending rather than saving this newly acquired income has been promoted and encouraged by policies issued by the Chinese government. Severe issues also confront China's domestic fruit industry, as it looks to face several acute demographic challenges in the coming years. Increased urbanization and industrialization have led to a steadily decreasing rural population over the past 30 years. An increasingly smaller and de incentivized population of young farmers and laborers is prompting concern about China's ability to satiate its own

¹⁸ Credit Suisse, Global Wealth in 2015: Underlying Trends Remain Positive, October 13, 2015.

¹⁹ Agriculture and Agri-Food Canada "Consumer Profile – China," September 2014.

consumers' ever-growing appetite for fresh fruit via domestic production. Fresh fruit imports look to fill this demand-and-supply gap. Coupled with continued apprehension toward domestic food safety and the rising trend of healthy and organic produce, increased consumption by China's growing middle class looks to ensure the continued success of foreign fresh fruit imports in China for at least the near future.

6.1.2 Prestige of Foreign Imports

Imported produce and fresh fruit, especially of Western brands and products, continue to remain symbols of status or wealth for many middle-and upper-income Chinese consumers in not only Tier I cities, but increasingly Tier II and III cities as well. Consumers are also becoming hungrier for expanded variety in fresh fruit and vegetable imports, especially of the tropical category. Foreign fresh fruit exporters can take advantage of China's domestic growing seasons and counter-seasons. In the winter months, domestic fruit production is severely limited, and as a result consumers who normally buy domestic turn to higher-priced fresh fruit imports. Even though the majority of Chinese consumers remain quite price-sensitive in their purchases of fresh fruit, this growing segment of middle-and upper-income white-collar professionals in Tier I, II, and III cities are determined to buy foreign regardless of higher pricing. Imported branded fresh produce is also perceived as meeting higher food safety standards and thus demands a premium in the Chinese market.

6.2 Healthy Foods and Food Safety

Chinese consumers traditionally place high value on fresh fruit as a method of staying healthy, prizing its health benefits. A growing segment of the population has become more concerned with food safety standards and regulations; domestically grown fruit is widely considered to be of a lower quality and have inferior safety standards as compared with foreign imported fruit. This has been compounded in recent years by an increase in the number of food scandals in China, ranging from melamine-laced baby formula to contaminated frozen strawberries and juice made from rotten apples and pears. Public exposure of these incidents has been aided by the explosion in popularity of social media in China. Although Chinese food safety regulations have been greatly expanded and improved in the past decade, Chinese middle-and upper-income consumers continue to prefer foreign fruit imports due to (real and perceived) superior food safety standards, usage of natural ingredients, and absence of chemicals and pesticides. Food products with a health and wellness focus are forecasted to enjoy continued high growth rates into the 2020s, and by aggressively marketing exported fruit brands as of a certifiably high quality with minimal pesticide/chemical use, exporters of fresh fruit to China can maintain certain competitive advantages over domestic producers and other foreign competitors.²⁰

6.3 Direct Export to Tier II/III Cities

Transportation infrastructure and end-to-end cold chain logistics continue to improve in China, especially in Tier II and III cities and spurred on by increasing consumer demand and government and

20 Andrew Kuiler and Erica Penzien, "Chinese consumers demand healthy food imports," The Silk Initiative, February 24, 2015.

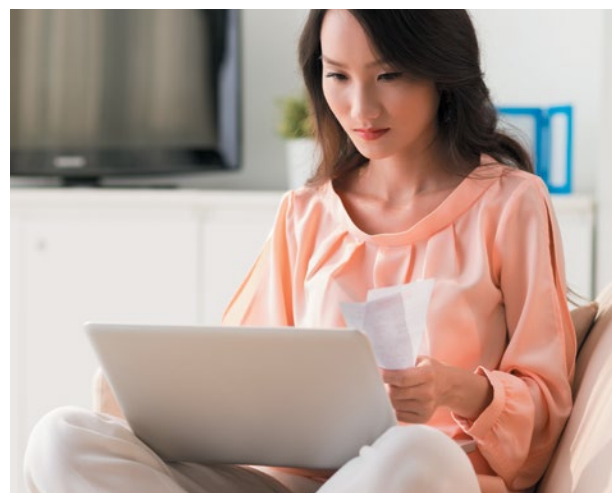
private investment. Currently, fresh fruit exports enter China via wholesale markets in Tier I cities and are transported by truck through a generally broken and marginally refrigerated cold supply chain to markets further afield in China. However, instances have begun to appear of direct distribution from Shanghai/Guangzhou to markets in Tier II and III cities by plane. This method can provide complete transit times from country of origin to Tier II/III markets within 48 hours, preserving product freshness and ensuring prompter delivery; shipments of Rainer cherries from Washington state in the U.S. began utilizing this method in June 2015 to great success.

Chinese importers, distributors, and wet/wholesale markets in these developing Tier II and III markets would prefer to go one step further and place fresh fruit import orders directly with the foreign exporter, eliminating the need for the produce to go through Shanghai or Guangzhou. Customs regulations and transportation difficulties currently hamper this, but as infrastructure develops in these regions, so do the possibilities for direct-to-Tier II/III fresh fruit imports. Chartered deliveries direct to Tier II cities have begun to gain in popularity—Zhengzhou, the capital of Henan province in central China, operates as distribution center of Chilean cherries for Beijing and Shanghai with the charter flights, and Qingdao has begun to receive direct container shipments of Chilean produce via sea.

Together with the expansion of supermarkets, hypermarkets, and other fresh food chains and boutiques in these cities, the opportunities for foreign fresh fruit exporters in less-developed and unexplored imported fruit markets in China’s vast interior are certainly not insignificant.²¹

6.4 Fresh Produce E-Commerce

Internet penetration continues to skyrocket in China, as its online population reached a total of 688 million users in 2015, with the largest growth rates amongst the population of mobile Internet users (610 million). E-commerce is witnessing similar growth as China’s online shopping population rose to 390 million in 2015 and is estimated to reach 500 million by 2018. Fresh produce e-commerce is predicted to rise to \$15 billion in 2017, a 350% increase over 2014 (\$4.3 billion).²² Sales of fresh fruit online have surpassed retail growth rates, spurred on by interaction



with consumers via online giveaways, promotions, and special e-commerce shopping holidays. Alibaba broke all previous e-commerce retail sales records in November 2015 during China’s unofficial national online shopping day, Singles’ Day, surpassing \$14 billion in total sales over a period of only 24 hours.

²¹ USDA Foreign Agricultural Service, “China – People’s Republic of: Fresh Deciduous Annual Report 2015,” GAIN Report #CH15059, November 16, 2015.

²² Fruit Day, How Online is the China Market? December, 2015.

Fresh fruit exporters can ensure successful online exposure to consumers and increased e-commerce sales through extensive brand building and marketing campaigns targeted at the most prolific purchasers of fresh fruit online in China. A 2015 Nielsen fresh e-commerce white paper found that the average fresh food online shopper in China is female, 33 years old, married, a white-collar worker, and well educated. Across all fresh food categories, 51% of shoppers purchased their fresh fruit online, and while they tended to purchase fresh produce only half as frequently as traditional offline shoppers, on average they spent twice as much on online fresh produce. The study also revealed that the primary motivation of 79% of surveyed consumers in shopping for fresh produce online was the greater level of freshness they considered e-commerce to provide, followed by convenience of purchase and delivery (74%) and greater options concerning product origins and imports (74%).²³

Partnering with fresh e-commerce companies in China who have a core, loyal consumer base and can provide services tailored toward these consumer segments can help foreign exporters distinguish their fruit exports and promote their brands amongst an increasingly cluttered and competitive online fresh fruit market.

6.4.1 Cross-Border B2C E-Commerce

Cross-border B2C e-commerce refers to a form of B2C (business to consumer) online purchasing whereby consumers can purchase foreign goods²⁴ online via e-commerce platforms and marketplaces, such as kijt.com, Tmall Global, and others, who are set up to operate within special Free Trade Zones (FTZs) in China. Mainland China's first FTZ was the Shanghai FTZ (SHFTZ), designated as such in 2013. Despite slow progress, this has since facilitated the growth of e-commerce sales by eliminating the need for imports to go through lengthy customs inspections and border processes, which can degrade quality and freshness in the process, while at the same time combatting smuggling, counterfeiting, and evasion of customs duty. Vendors are preapproved by the GACC and products sold and shipped through the Shanghai FTZ are rapidly processed and delivered to their destination within China. The Chinese government has recognized the immense potential for e-commerce, especially among agricultural and fresh fruit imports, and has offered support and stimulus in the form of reduction in tax rates, tariff reductions, and support for logistical development. Based on the success of the 2013 SHFTZ, three new FTZs were opened in April 2015 in Tianjin, Fujian, and Guangdong, and the Shanghai FTZ was expanded to encompass 120 square kilometers.

Recent developments have cast an uncertain shadow as to the future of fresh produce cross-border e-commerce in China. Previously, selling fresh fruit via cross-border e-commerce provided substantial benefits not found in standard import-export trade, such as tariff and VAT waivers for purchases made under 500 RMB (\$80) and lower customs and duty rates for other purchases (10% for foodstuffs). Under this regime, fruit exports that had high tariff rates and exports from countries that had yet to conclude FTAs with China benefited greatly by the significant reductions in tariff and VAT rates. A prime example

²³ Nielsen. Fresh E-commerce Development White Paper. October 30, 2015.

²⁴ Which have already been granted market access in China.

of this was Mexican avocados which, due to their high tariff and VAT rates due to no FTA with China, were at a significant pricing disadvantage compared to avocados from Chile or Peru. Previously, this could have been alleviated by selling via cross-border e-commerce and benefitting from tariff and VAT waivers, increasing the price competitiveness of Mexican avocados in China, but now Chilean and Peruvian avocados have regained the upper hand in terms of pricing competitiveness as a result of tax and policy changes.

In March 2016, China's Ministry of Finance (MOF) announced sweeping changes of permissible products and tax rates for goods imported via cross-border e-commerce, which excluded fresh produce, effective April 7. This was amended by the April 15 release of a second positive list by the MOF, which allowed fresh produce once again to be imported via cross-border e-commerce, but still kept changes to import duties and VAT. Cross-border B2C e-commerce operators must now pay 70% of the assessed VAT rate even if import duties are 0%.²⁵ This new rate is assessed on retail prices as opposed to import prices, invalidating the previous 0% for purchase made under 500 RMB and duty rates of 10% overall for foodstuffs, significantly increasing the cost associated with fresh produce cross-border B2C e-commerce.²⁶ Cross-border e-commerce's situation and future in China remains relatively volatile, and future updates to the laws governing the tax rates and permissible products made by the MOF have the potential to either hamper or encourage growth of this form of fresh produce e-commerce.

7. Future Challenges

7.1 Market Access Challenges Due to Technical and Political Issues

Significant technical and political barriers in exporting to China still exist and limit access to the Chinese market. The process of applying for market access is highly variable in China, with the entire process ranging from between 2–3 years to 10 years or more. Not all fresh fruit products and countries are allowed market access in China; as of February 2016, 39 countries were allowed to import specific categories of fruit into China. Allowed and disallowed product categories are reliant on both technical and political limitations, with quarantine and pest control the major factors influencing technical admittance of imports into China. AQSIQ has established strict inspection regulations to safeguard domestic Chinese produce against possible pest infestation and fruit diseases. AQSIQ procedures can be slow and require large amounts of back and forth on the part of the importer/exporter and the AQSIQ.

Political factors outside of the control of the exporter can greatly hinder success in China. Countries with FTAs enjoy significant competitive advantages in the Chinese market, such as low or nonexistent tariffs, enabling these products to be sold at a lower price as compared to products from countries without FTAs with China. Exporters in some countries may have little leverage in encouraging their

²⁵ "Produce Added back to Positive List for Cross-border E-commerce," Guojiguoshu.com, April 21, 2016.

²⁶ "China Introduces New Tax System for Cross-Border E-Commerce," Producereport.com, March 31, 2016.

own governments to open FTA negotiations with China, as concluding FTAs with China can be a rather controversial move in some countries.

Product market access can also change amid changes in the political landscape. In 2012, exports of bananas from the Philippines to China were restricted on the basis of health violations and pest control; however, many saw this as a part of the ongoing dispute concerning contested territory in the South China Seas, with the Chinese government imposition of restrictions on Philippine bananas a retaliatory measure for their refusal to acquiesce politically. To overcome these substantial challenges, exporters must work together as an industry group in their home country to lobby their government to take the lead on opening bilateral dialogue with the AQSIQ and relevant Chinese authorities. Acquiring and maintaining good bilateral relations greatly helps in achieving market access; nevertheless, this may be very difficult for foreign exporters to influence, and even then, technical (quarantine, pest) concerns may easily be brought up as grounds for blocking market access if significant problems persist in the political relationship between countries.

7.2 Intellectual Property Protection

A major concern for any foreign exporter in the China market is the protection of their Intellectual Property Rights (IPR). Imports of foreign fresh fruit are currently one of the most infringed-upon product categories. As consumer demand for fresh fruit and vegetable imports increases, incidents involving fake labeling of cheap, domestic fruit as premium foreign imports have increased as well. Examples of these incidents include the 2015 discovery of Chinese grapes and dragon fruit in several Shanghai markets with falsely affixed Zespri labels and the April 2014 seizure by customs officials in Hong Kong of over 5,000 North African oranges with counterfeit Sunkist labels being sold at 400% their intended price, seized following consumer complaints of oranges “thicker and more sour than usual.” These are only two of the numerous examples of IPR infringement involving foreign exports of fresh fruit in China. Incidents like these not only diminish the exporters’ profits, but more importantly cause damage to the brand reputation of the exported fruit, and can cause a consumer to become more wary of and hesitant to purchase fresh fruit exports of that particular brand.

Exporters are highly advised to register their intellectual property before entering the Chinese market and apply for the proper trademark, copyright and patent registration. Exporters are also encouraged to acquire local legal counsel upon suspicion of IPR infringement and aggressively protect company trademarks, such as cease-and-desist actions and involvement of the proper Chinese authorities. Consumer education should be focused on as a means to help provide consumers with the necessary tools to be able to distinguish between real and counterfeit fruit imports. Conducting public relations campaigns via social media, traditional media, and in-store tastings can provide consumers with the necessary information, such as product variety, general size, texture, color, and where licensed

distributors and retail outlets for your product are located, in order to both increase consumer awareness of a particular export as well as making them more wary toward counterfeit fruit imports.

7.3 Distribution and Cold Chain Challenges

Insufficient and inefficient distribution networks and cold chain supply management remain major obstacles hindering expansion of foreign fresh fruit exports to China, especially to destinations in China’s interior. Total cold chain logistics penetration in China was estimated in 2014 to be roughly only 19%, compared to 85–90% in countries such as Japan and the United States.²⁷ Deficiencies in cold chain transportation, storage, packing, and preservation methods lead to large product losses; it is estimated that fresh fruit incurred a 20–30% loss rate in 2014, equaling 12 million tons of fresh fruit with a total value of over \$16 billion.²⁸ Despite rapid sectorial growth since 2008, China’s fleet of refrigerated trucks totaled only 50,000 in 2015, with a Rabobank report estimating that \$85 billion in investment is needed over the next 10 years in order for China’s cold chain sector to improve both in terms of quality and capacity.²⁹



China’s vastness compounds existing problems. Cold chain infrastructure outside of China’s major cities and import hubs remains underdeveloped where most of China’s advanced cold chain transportation is located. Due to their close proximity to import ports and relatively developed cold chain infrastructure, delivery times in and around Tier I cities are short, allowing distribution to be satisfactorily conducted via air-conditioned trucks outfitted with ice bags and packs (instead of refrigeration units) to save on costs. Despite recent logistical and technological improvements, long-haul refrigerated trucks servicing Tier II, III, and IV cities continue to suffer from inconsistencies in distribution quality as well as temperature management. There also exists a lack of clear and concise regulations and enforcement in cold chain logistics, which when coupled with the absence of standardized health and safety regulations regarding temperature and handling requirements of fresh fruit, lead to decreases in product quality and increased consumer distrust.³⁰

Cost-cutting measures remain the bottom line for smaller Chinese cold chain distributors, especially those servicing China’s interior. Imported fruit shipped from wholesale markets to Tier II and III cities often are non-refrigerated in order to save on costs associated with refrigeration units and oil and gas for the trucks; only for high-value products and during the hot summer months are refrigerated trucks

²⁷ Bamboo Innovator, 2014.

²⁸ International Trade Administration, U.S. Department of Commerce, 2015 Top Markets Report Cold Chain, May 2015.

²⁹ Margo van Wijgerden, “Mind the gap – investment in railway cold chains required to meet China’s demand for perishable food,” Rabobank. October 28, 2015; University of Nottingham, 2015.

³⁰ ITA Top Markets Report Cold Chain, 2015.

utilized. For short-haul distribution, this does not necessarily have an adverse impact on the quality of certain produce, but for some temperature-sensitive produce transported over longer distances via non-refrigerated trucks, product quality can be drastically affected. This practice is slowly being remedied by the introduction of temperature-monitoring devices and increased efforts in training and education for cold chain logistics operations and management personnel.

Advances are being made in cold chain management and networks, and year-over-year cold storage industry growth rates in China are growing 25% annually, with the cold chain logistics sector expected to be worth more than \$74 billion by 2017.³¹ Increasing consumer demand is expected to stimulate investment in B2C e-commerce cold chain logistics, with growth rates over the next decade forecasted at between 80 and 120% per annum, primarily stimulated by direct investment into upgrading cold chain infrastructure and distribution by China's major online retail and e-commerce giants. The Chinese government has begun to take a more active role in regulating and promoting cold chain logistics, issuing a logistics industry development plan until 2020, focusing on standardization and modernization of current practices. Finally, growing consumer awareness of and concern for food safety issues have facilitated a dramatic increase in the demand and utilization of cold chain warehouse and transportation systems in Tier I, and increasingly Tier II, cities.

7.4 Business Culture

Despite increasing modernization and development, Chinese business culture can prove challenging for companies acclimated to Western business practices. As a result, finding a suitable business partner (distributor/importer/retailer) in China can be a monumental task for some exporters. Business practices in China are generally less argumentative, with businessmen eager to agree and make arrangements or promises they may be unable to satisfy or keep. Foreign companies accustomed to open dialogue and direct negotiation can be frustrated by their Chinese business partner's often disorganized, non-direct, and non-confrontational ways of conducting business. Many new and emerging companies are ignorant of or pay little attention to the branding of their own companies, with a large number of these lacking company websites, especially those available in English. Many businesses, including importers, distributors, and retailers, often seek success in the short term with little thought being given to long-term strategy.

Communication barriers can be significant, sometimes requiring the use of translators and hindering relationship building. Although more and more Chinese businessmen are able to communicate to some degree in English, they often only possess a very basic knowledge of English and as a result, miscommunication is relatively commonplace. Foreign exporters must be diligent in ensuring that all communications are clearly understood by their Chinese partner(s). This can be achieved by the foreign exporter repeating their proposals/plans. multiple times, confirming that their partner is indeed at a mutual understanding, and conducting comprehensive follow-ups. It is important that exporters

³¹ Van Wijgerden, 2015.

entering the Chinese market are aware of other, sometimes specifically regional or cultural, differences, and enter the market with expectations adjusted accordingly.

8. Recommendations to Companies Wanting to Export to China

8.1 Strict Compliance with Import Protocols

To avoid market access delays and rejection of product for import, foreign fresh fruit exporters should resolve to strictly comply with Chinese import laws and protocols:

- Market access laws and regulations issued by Chinese government agencies should be closely followed
 - Import procedures specific to the China market should be observed
- All relevant documentation and comprehensive technical information should be submitted in a timely manner to the relevant customs authorities
 - Special attention should be given to fulfilling AQSIQ requirements and providing additional information as required
- Contacts should be established with sub-agencies under AQSIQ, such as CIQ and CIQA, to create cooperation mechanisms and facilitate bilateral discussion
 - Conferences and seminars can assist in clearing up confusion related to import regulations and encourage quicker market access into China
- Resources, guidelines, and export reports for produce exports to China of the exporting country's embassy, agricultural department, and/or local, state, national government should be utilized

8.2 Network and Relationship Building

Building networks and maintaining relationships are crucial in achieving success in the Chinese imported fresh fruit market. Importers, distributors, agents, and all other Chinese partners should be carefully researched and selected in order to avoid potential poor product handling, cold chain management, and retail execution. It is important to stay in constant communication with your Chinese partners and conduct trips to China to meet with distributors/agents—these both develop and maintain *guanxi*, or mutually beneficial relationships. Exporters should be prepared to spend much more time, effort, and money in cultivating these relationships than they might with similar partners in Western markets. Constant effort is required from exporters and their supporting industry groups and/or provincial/national governments to keep close working relationships with AQSIQ, its experts, and other Chinese customs officials. Cooperative mechanisms should be established between countries, and official visits conducted between both parties at both an industry and official level.

8.3 Thorough Market Research Analysis

Entering the Chinese imported fruit market can be a daunting proposition for some smaller fresh fruit exporters. It is important that the proper research and analysis is conducted to prepare for market entry specific to the circumstances of each foreign exporter separately. These can include:

Identifying and resolving possible market access issues and barriers to trade

- Permissibility of specific fruit imports from specific countries
 - Status of bilateral FTAs with China and amount of tariffs and duties to be levied

Determining export region in China based on:

- Necessity of complete cold chain management and well-established distribution networks to decide between Tier I/II/III/etc. cities
- Consumer demographics, such as age, income, marital status, etc.
 - Younger, middle-to high-income families are more likely to buy imported fruit due to concern about food safety and organic food
 - Level of consumer awareness and familiarity with your export or any preexisting consumer fruit preferences

Determining export season and varieties

- During certain seasons/time periods, exports of particular foreign fresh fruit experience heightened demand
 - These can include sales of brightly colored fruit in advance of certain Chinese holidays, or during Chinese domestic fruit counter-seasons
- Suitability of certain fruit exports to China
 - More difficult to maintain product freshness for particular varieties of fruit given lengthy transportation distances, especially if export origin is far from China

Determining method of sale channels

- E-commerce, supermarkets, hypermarkets, specialty or boutique stores, wet/wholesale markets

It is highly advisable to retain a degree of flexibility in approaches taken toward the Chinese market. Foreign fresh fruit exporters should also utilize the resources provided in their home country, such as trade and industry associations, foreign embassies in China, trade commissioner services, chambers of commerce, or other similar governmental services, which can provide assistance in risk management, financial services, and up-to-date trade information.

8.4 Educating Chinese Trade and Consumers

Establishing and maintaining one's brand and reputation is key in achieving long-term success in China's imported fruit market. Before entering the China market, foreign exporters should examine their brand and take the necessary steps to tailor it for Chinese consumption. The imported fruit market in Tier I cities (and increasingly in Tier II cities) is highly competitive, but international brand awareness among Chinese consumers remains very limited, with only three foreign brands widely recognizable by the average consumer: Zespri, Sunkist, and Dole. Therefore it is critical for other foreign brands looking to enter the China imported fruit market to commit to extensive branding and marketing activities in China, first with Chinese trade and industry groups, followed by consumers and consumer groups. These activities can include:

- **Attending trade shows, technical seminars, and hosting media events to promote trade and industry awareness within China**
- **Utilizing Chinese trade media websites and platforms to educate targeted Chinese trade and industry groups about your product and brand**
 - Produce Report and similar platforms present effective channels to reach, educate, and connect with a large audience of trade and industry groups in China
- **Expanding consumer awareness via Chinese social media outlets**
 - Weibo (Chinese Twitter) and WeChat (Chinese Facebook) have hundreds of millions of active users and can provide an excellent location to carry out consumer awareness campaigns, conduct product giveaways, and other activities
- **Highly advertised in-store promotions and marketing in partnership with retail outlets**
- **Pre-sales marketing campaigns in collaboration with popular e-commerce sites**
 - Generates increased interest and demand via both social media and word of mouth

Some fresh fruit exporters start at a disadvantage in the China market, as Chinese consumers generally give preference to imports from North America/Europe over other parts of the world, rooted in the prevailing stereotype that a Western product automatically equals a good one. This is a significant challenge for exporters from other developed and developing countries seeking to expand their fresh fruit exports to China. These countries must broaden their efforts in China and plan region- and country-wide public relations campaigns focusing on educating consumers as to the fruit's country of origin. Successful "Made in" campaigns can increase consumers' opinions and perceptions of a specific country, and make them more favorable to fresh produce exports from that country.

Once market access has been successfully achieved, product trend monitoring and constant brand refreshes and updates should be continued in order to maintain relevancy. Resting on one's laurels after having achieved a reasonable degree of success almost guarantees failure in the fast-paced and ever-shifting Chinese imported fresh fruit market.

9. Conclusions

Despite slowing growth rates and growing uncertainty as to the health of China's economy, the imported fresh fruit market in China looks to maintain and even exceed its impressive growth rates of the past decade. China remains a large market with huge, untapped potential, especially in Tier II/III cities and among an ever-expanding middle class with access to rising disposable income and increasing appetite for foreign fresh fruit imports. Driven by rapidly developing e-commerce, foreign fresh fruit exports to China will continue to grow in scope and profitability, with exporters who expend the time and effort to explore, develop, and promote their presence and brand in China to be rewarded with sustained long-term profits.



10. Appendix

China's Free Trade Agreements by Country: Completed, Under Negotiation, and Under Consideration

COUNTRY	YEAR INITIATED; YEAR SIGNED (if applicable)	CURRENT STATUS
ASEAN (includes Brunei, Burma, Cambodia, Indonesia, Laos, Malaysia, Philippines, Singapore, Thailand, Vietnam)	2002; 2010	Signed and in force
Australia	2005; 2015	Signed and in force
Chile	2004; 2005	Signed and in force
Colombia	N/A	Under consideration
Costa Rica	2008; 2011	Signed and in force
GCC (includes Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, UAE)	2004;	Under negotiation
Georgia	2015;	Under negotiation
Fiji	N/A	Under consideration
Iceland	2007; 2014	Signed and in force
India	2006;	Under consideration
Japan, South Korea (tri-lateral)	2010;	Under negotiation
Maldives	2015;	Under negotiation
Moldova	N/A	Under consideration
Nepal	2016	Under consideration
New Zealand	2006; 2008	Signed and in force
Norway	2007;	Under negotiation
Pakistan	2005; 2009	Signed and in force
Peru	2007; 2009	Signed and in force
Singapore	2008; 2008	Signed and in force
South Korea	2006; 2015	Signed and in force
Sri Lanka	2014;	Under negotiation
Switzerland	2011; 2014	Signed and in force