



Companies race for rice market supremacy

by David McKee

COFCO, Wilmar International look to invest in bigger and more efficient mills in China's key production areas

China produces over 190 million tonnes of paddy rice per year, most of which is traditionally processed at the township level by up to 100,000 mills. It is the largest staple food crop grown and consumed in any country.

Now urbanization, rising incomes, rural policy changes and unrelenting modernization and corporatization of grain milling are bringing accelerating change to how rice is produced, processed, distributed, marketed and consumed in the Middle Kingdom.

Once largely neglected by the giants of the country's food industry, in the last few years rice milling has come to be viewed by them as a key driver of medium- and long-term growth.

The two largest agribusiness companies in China — China Oil and Food Corporation (COFCO) and Wilmar International — have engaged in an intensifying race to invest in bigger and more efficient mills in key rice-producing areas. At the same

time, they are pouring equal amounts of financial resources into building rice brands with nationwide distribution among the largest retail supermarket chains like Carrefour and Walmart.

Singapore-based Wilmar International entered the rice sector less than three years ago but has already built six new large mills, with several more on the drawing board.

COFCO has responded by investing in new capacity of its own, both in the Northeast and south of the Yangtze, as it promotes a family of national brands. The state-owned company had a traditional role as China's main exporter and importer when such trade was more heavily regulated and operated rice

(Above) Point of sale displays and colorful packaging are evidence of the intense competition in retail rice marketing in China. Fragrant Thai jasmine rice is gaining popularity among well-to-do consumers. Photos courtesy of David McKee.

mills for this limited scope. Now it is being asked by the highest level of government to act as a national champion in what is still considered to be an economic sector of vital strategic interest.

Rice is only the latest chapter in a rivalry between COFCO and Wilmar that extends back nearly a decade, which is considered a lifetime in the fast-moving world of Chinese business. Wilmar and COFCO already dominate production of edible oil in China. The two companies started out as partners together with U.S.-based Archer Daniels Midland in the huge build up of coastal soybean crushing capacity in China. About eight years ago they began pursuing separate investment strategies in part to comply with Beijing's wish for greater competition in the sector. Subsequently, Wilmar bought out ADM and engineered a merger in 2006 with Kuok Oils, Malaysia to create the largest agribusiness company in Asia, with \$24 billion in 2009 sales revenues and \$1.9 billion in net profits.

Industry sources report that Wilmar has been unofficially restricted from increasing its share of the edible oils industry in China. This has left enormous cash flow to invest in rice milling as well as wheat flour milling, another sector in which Wilmar is also mounting a challenge to COFCO's traditional leadership. Publicly traded Wilmar already reports over one million tonnes of combined rice and wheat flour sales in 2009. Though a newcomer that has built its own production from scratch, Wilmar has leveraging its huge edible oils distribution network.

INDUSTRY STRUCTURE

One of the new mills built by Wilmar in Heilongjiang has daily capacity of 1,200 tonnes, while the others are 600 tonnes per day, now the standard size for Wilmar's greenfield sites. COFCO used to operate only relatively small mills, but the competition has forced it to build bigger capacity as well. Its typical new plant is now 800 tonnes per day, according to one mill equipment manufacturer, though for small-grained rice it still puts

up 300 tonne-per-day mills.

Corporations with large-scale mills and national distribution of their brands may now account for 20% to 25% of the rice milled in China, according to several sources. There are around 25 such companies.

Industry insiders report that village mills doing just five or 10 tons per day have mostly disappeared in the last five years. The remaining mills, numbering in the tens of thousands, fall within a capacity range of 50 to 200 tonnes per day.

Both Wilmar and COFCO have invested heavily in mills in the northeast, because it is a rice surplus area. The rice zone contained within Heilongjiang, Jilin and Liaoning provinces is distinct in a number of ways from the major production areas south of the Yangtze River. Opened up to Han Chinese farmers relatively late in Chinese history during the Qing Dynasty when it was known as Manchuria, farms are larger and more mechanized. The Japonica rice variety grown there is reputed for its flavor and is gaining favor and distribution throughout China.

The northeast is home to another top player in China's rice industry, a state-owned, diversified agribusiness concern called Beidahuang Group, with headquarters in Harbin, Heilongjiang Province. Its rice subsidiary has rapidly expanded throughout China and now operates mills in five provinces including Guangdong, Shanghai and Jiangsu, with total yearly rice milling capacity of 3 million tonnes.

Also among the top four rice millers in China is Jinjian Rice Company based in Hunan Province in central China, just south of the Yangtze River. It has the most extended geographic coverage, operating mills in Heilongjiang in the far north, Hainan in the far south, and inland in Sichuan Province. Products include rice bran oil and instant rice flour.

About 20 smaller companies with national aspirations make up a second tier in the corporate milling sector.

RICE MARKETING AND CONSUMPTION

The old rule was that northern Chinese consumed wheat-based foods like



In a supermarket in Beijing's Chaoyang District, COFCO merchandisers run a special promotion of the company's Qiheyuan ("Source of Seven Rivers") brand.

noodles and steamed rolls, and southern Chinese ate rice. For centuries, the Middle Kingdom has been the world's biggest producer of both grains. In rural areas these eating habits may still mostly hold true, but in the country's burgeoning cities, diets are increasingly varied.

Supermarket shoppers in northern cities may notice that attractively packaged rice occupies more and more shelf space.

Sacks of wheat flour are less and less present, as harried urban consumers have little time to prepare wheat-based foods at home, though noodles of all types and frozen steamed rolls and dumplings are gaining space in the same supermarkets.

Urban consumers are demanding higher quality rice and paying a premium for it. Thus, branding strategies have become critical in rice marketing. There are many hundreds of rice brands sold in China. At least 40 of them have been certified as a "famous China brand" by a national business association.

Wilmar and COFCO have applied their blanket Jinlongyu and Fulinmen brands respectively to their broad range of packaged foods, and COFCO has even named its modern new headquarters office tower in Beijing the Fulinmen Plaza.

Defying trends seen in neighboring countries that have experienced rapid income growth, in China total milled rice consumption has been holding steady at between 115 million and 120 million tonnes per year, or about 90 kilograms (kg) per capita, over the last five years, according to independent data obtained from Beijing-based agricultural consultancy BOABC. South Korea, on the other hand, has seen its per-capita rice consumption drop by over one-third to 70 kg in the last 30 years.

One explanation is that rice is gaining share of stomach against wheat-based foods. In the past 30 years, tens or even hundreds of millions of young workers have migrated from poor inland and northern provinces to work in factories in the booming southern coastal regions before returning home after a few years. Many acquired a taste for rice that has stayed with them.

Urban Chinese families eat out much of the time, and many single people in cities rarely cook for themselves. Restaurants and institutions in northern cities are more likely to serve rice

these days. Vast improvements in road and rail infrastructure have lowered transport costs to these cities from distant rice-growing areas.

RICE PRODUCTION AND PROCUREMENT

To augment rural incomes and ensure sufficient rice production, the Chinese government has repeatedly increased the floor price paid to farmers. For early long-grain Indica rice grown in the south, the 2010 floor price is 1860 yuan (\$272) per tonne, and for the short-grain Japonica rice purchased from July to November it is 2,100 yuan (\$307) per tonne. This has resulted in a greater share of the crop being purchased by the government authority Sinograin and added to the state reserves. China's economic stimulus spending measures have included the construction of new rice storage facilities for state reserves.

More state procurement may be helping to speed the consolidation of milling into the hands of large corporations. In order to rotate its stocks, Sinograin sells at auction the rice it has bought from local farm commodity exchanges. The big corporate rice millers with their lower operating costs, deep pockets and sharper pencils are better positioned to outbid their smaller rivals and make cash payments for large quantities sold in this manner.

Since 2004, rice and other grain growers have benefited from direct payments and subsidies for fuel, fertilizer and seed. Also, most agricultural taxes have been eliminated. One USDA report cites an informal survey from one northern region that showed 30% of rice farmers' profits resulted from these subsidies and payments.

Despite this government support, rice farming remains a subsistence activity for many households. By some estimates, as much 30% of paddy rice may still go to farmers' own consumption. The households take their rice to local operators for toll milling in the informal non-cash economy.

Average rice yields in China, at 6.5

tonnes per hectare, are among the highest in the world and are still going up, though at less than 1%.

Official data is lacking, but there is strong evidence that low-quality rice, along with wheat, has been replacing expensive maize for use as animal feed in recent years. USDA estimates 11 million tonnes of early-season rice and rancid stocks from government reserves went for this purpose last year, while BOABC's estimate is 9 million tonnes.

INTERNATIONAL TRADE

Thanks to government farm support to meet national food security and rural development policy goals, China's rice market is well insulated from international influences. Per recent USDA reports, imports are limited to just 300,000 tonnes, almost entirely fragrant Thai rice that is sold to hotels and restaurants and in supermarkets to high-income consumers. Japanese companies have invested in rice mills in northeastern China to improve the quality of Japonica rice milled there. China's rice exports now consist almost entirely of this variety going to Japan and South Korea, estimated by USDA to amount to 900,000 tonnes in the current year. BOABC's estimates are higher at 600,000 tonnes of imports and 1.5 million tonnes of exports. Prior to the food price crisis of 2008, China encouraged exports of low-quality Indica rice to Africa through VAT rebates. But this policy was revoked to protect the domestic market from price increases.

World markets are an inconsequential sideshow for China's rice industry. The main spectacle is the battle for domestic market domination now taking place between national champion COFCO and Asian agribusiness behemoth Wilmar. WG

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