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China Drinking Water Industry Report, 2009-2010

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2. China Drinking Water Industry

2.3 Market Analysis

2.3.3 Dual Water Supply

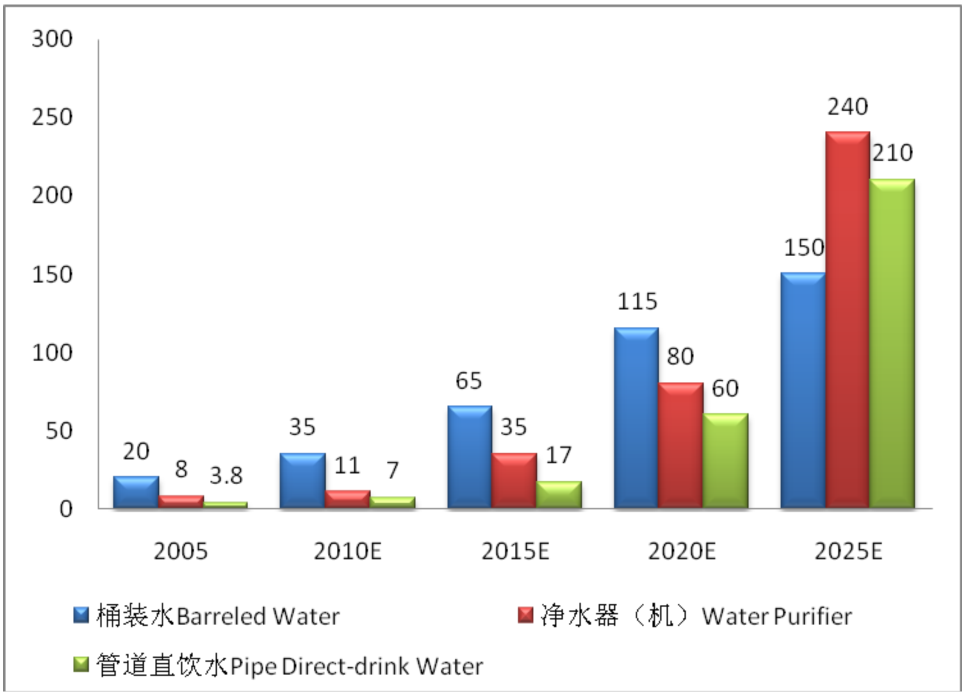
Bottled (Barreled) pure water, household water purifier, pipe direct-drink water are totally called dual water supply. In the beginning of 1980s, bottled pure water entered Chinese market, and developed to be bottled (barreled) water, water purifier, and pipe direct-drink water, which promoted the development of water purification industry (materials, film technology, equipment, device and accessories). At present, there are problems with water market regulation and technological development.

In July 2008, General Administration of Quality Supervision, Inspection and Quarantine of PRC issued the spot-check results on the 148 kinds of bottled drinking water quality produced by 145 enterprises in 20 provinces and cities such as Beijing, Hebei, Shanxi, Heilongjiang, Shanghai, Jiangsu, Zhejiang and Henan. The examination was made on 101 kinds of pure water, 32 kinds of natural mineral water and 15 kinds of drinking water, and the results displayed that the qualified rate of large-scaled manufacturers with large market shares was 95.7%, and the products quality was relatively good. The overall quality qualified rate was 87.2%. With strengthen of supervision, the qualified rate of bottled (barreled) pure water was improved gradually, which created satisfied consumption environment for consumers.

In future 15 years, the demand for bottled water will be up steadily, but limited by transportation and short quality guarantee period, the future new water supply way will change the consumption idea. Till 2025, the market space of bottled water will shrink gradually, while water purifier will become the main force of dual water supply for its flexible installation and wide application.

Integrated by multi-science and multi-technology, pipe direct-drink water will develop with national economy and urbanization progress, and enter rural areas with integration of urban and rural areas. Till 2025, its market share will exceed that of barreled water.

China Dual Water Supply Output and Growth, 2005-2025 (Unit: million m3)



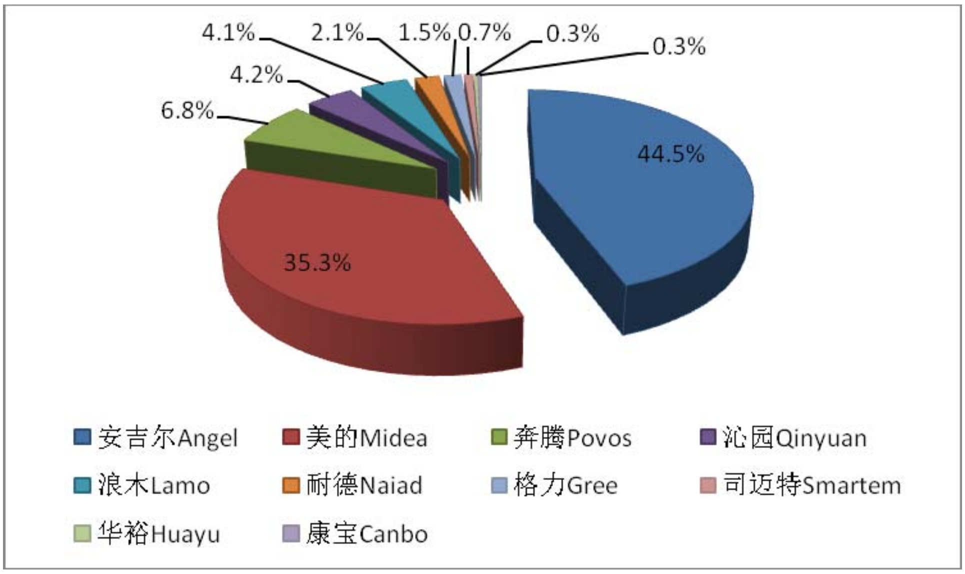
Source: ResearchInChina

3. Development of China Drinking Water Related Industries

3.1 Water Fountain Market

At present, the population of water fountain in China has exceeded thirty million sets, of which 20% or about six million sets needs to be replaced annually. The great demand and high profit of water fountain market lead to price wars.

Market Share of Water Fountain Brands in China, 2009 (%)



Source: ea3W.com, ResearchInChina

It can be seen from the above figure that Midea and Angel take larger share of Chinese water fountain market, nearly 80% altogether whether in sales, sales volume or in brand and retailing.

4.2 Bottled Water Market

4.2.1 Development History

In 1930, Germans opened the first Laoshan Bottled mineral water plant in China, producing the bottled water. This started up Chinese bottled water market in real sense. In 1992, Zhengguanghe, which produced soda pop, transfer part of production lines to the pure water industry, driving the bottled water market to enter the era of purified water manufacturing. In 1995 and 1996, the two dairy giants Wahaha and Robust accessed into the bottled water market in succession. Nongfu Spring, however, marched into the bottled water market by its excellent marketing capability in 1998, and Nongfu Spring, Wahaha and Robust altogether accounted for 40% of domestic market shares.

Entering the 21st centry, national bottled water industry has been in the stage of steady growth, taking a 40% share of all beverages. A variety of brands of purified water, mineral water, spring water, natural water and mineralized water mushroomed in Chinese market. With the rising cost of operation, packaging and labor force as well as the increasing fierce market competition, Chinese bottled drinking water industry has been in the stage of full competition. Huge foreign capital flows into Chinese bottled water market. It is only in several years that Danone has seized 60% of Chinese bottled water market shares. Under the backdrop of significant growth in the sales volume of purified water worldwide, Coca Cola and Pepsi Cola also set foot in the bottled drinking water market.

4.2.2 Status Quo

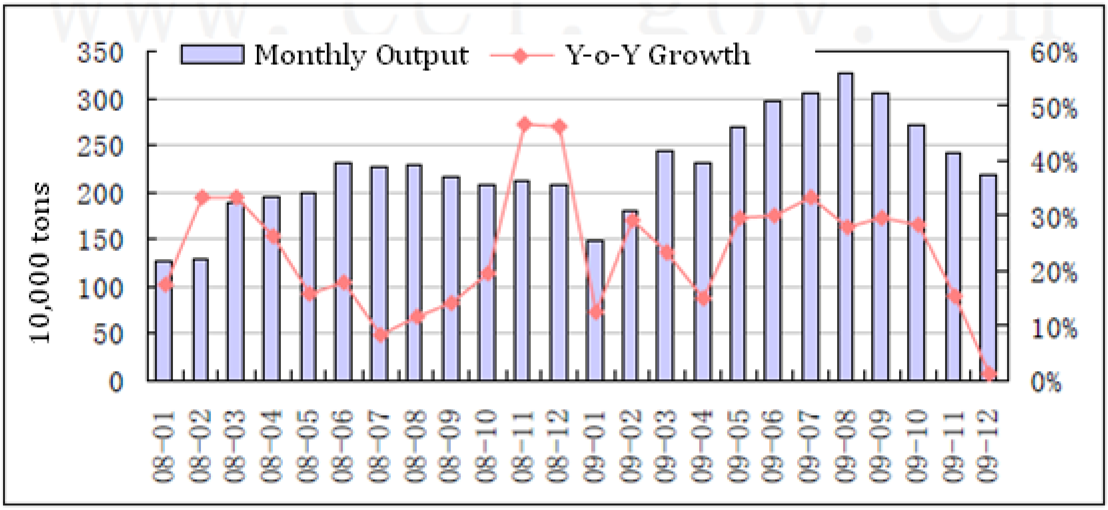
In current market of soft drinks, the output and sales of bottled drinking water ranks first and second respectively. Since huge market space, low entry threshold, and short period of investment returns, the bottled drinking water market attracts different investors. In 2008, China’s output value of bottled drinking water reached RMB39.5 billion.

In the past, the enterprises marched into the bottled water industry sucessively under the drive of economic benefit, which resulted in the oversupply of the whole industry. Low-price strategy is the main means in market competition during the recent years.

Of bottled drinking water, purified water and mineral water are the major two varieties; wherein, purified water is absolutely the leading force, while mineral water witnesses slow development. As a leader of purified water, the output of Wahaha amounted to 2.8465 million tons in 2007, followed by C-estbon with the output of 1.o616 million tons in 2007. Danone is a leading enterprise of mineral water, and its output in 2005, 2006, and 2007 all reached above 300,000 tons, and it exceeded 400,000 tons in 2007. In 2009, the output of bottled (Canned) drinking water increased rapidly. In Jan.-Dec., China produced 31.5903 million tons of drinking water accumulatively, up 24.60% year-on-year and with growth margin increasing by 0.67% from the same period of last year.

In Oct., 2009, China produced 2.7241 million tons of bottled drinking water, a 28.34% YoY rise and with growth margin up 8.59 % from the same period of last year. In Nov., China produced 241.83 million tons, up 15.39% year-on-year and with growth margin down by 31.10% from the same period of last year. In Dec., China produced 2.187 million tons of bottled drinking water, up 1.18% year-on-year and with growth margin down 45.25% from the same period of last year.

Monthly Output and YoY Growth of China Bottled Water, 2008-2009 (by Month)



Source: www.cei.com.cn, ResearchInChina

It can be seen from the above figure that China's output of bottled drinking water keeps increasing. In spite of a drop in growth margin, Chinese bottled drinking water market still characterizes huge growth potential along with the growing awareness of people's health and the increasing demand of people for safe drinking water due to environmental issue.

4.2.3 Demand Analysis

1) The total consumption of bottled water decreases as a whole. Judging from the behaviors of consumers, many of them reduce the consumption of bottled water. As is revealed from relevant investigation, consumers like the carbonated beverage most in summer, accounting for 59.5%; and bottled water only 7.3% (ranking fourth). In Winter, juice beverage is the favorite of consumers, taking 41.7%; and bottled water only 4.5%.

2) Variety Selection-tendency for mineral water

In the bottled water market, the leadership of purified water has been replaced by mineral water. According to investigations in seven largest cities across China, 48.9% of people have a liking for mineral water; and 30.1% for purified water; and 21% of consumers expressed that they did not care at all.

3) Brand Selection – led by three big brands

The three brands, i.e., Master Kong, Wahaha, and Nongfu Spring account for the overwhelming shares of the bottled drinking water market, according to the investigations.

Market ShareS of Bottled Water Brands, Dec.2005-Sep.2009 (Unit: %)

Brand	Dec.2005	Dec.2006	Dec.2007	Dec.2008	Mar.2009	Jun.2009	Sep.2009
Master Kong	5.9	11	18.1	17.7	17.3	21.1	22.5
Wahaha	16.9	15	17.2	18	18.7	17.4	17.3
Nongfu Spring	10.7	10.4	11.7	12.2	13.5	14.6	14
C-estbon	7.9	9	6.7	7.5	6.6	5.1	2.7
Coca Cola	5.7	5.7	4.2	3.9	4.2	4.4	5.4
Runtian	3.4	2.7	3.4	4.4	3.4	3.7	5.7

Source: AC Nielsen, ResearchInChina

4) Much Importance Attached to the Quality of Bottled Water. Over one-third of the interviewees take the drinking security of bottled water as the key consideration, and such factor is the third to brand and price factors.

4.2.4 Market Competition Pattern

The leading forces in Chinese beverage industry mushrooms in recent years, in particular tea drinks and juice exerting great effect on the bottled water market. Plus, there are numerous enterprises in the manufacturing of bottled water in China, leading an increasingly fierce competition in the market, especially the fight with each other by price wars for more market shares. This resulted in price slump from RMB3-5/bottle to RMB1/bottle or even less than RMB1/bottle. According to the results of the investigations, Wahaha, Robust and Nongfu Spring take the majority of bottled water market shares, and the consumers has a growing brand awareness when buying bottled water. Besides, the three brands also do their best to seize more market shares. For example, Nongfu Spring emphasizes the natural weak alkaline water. In the meanwhile, the high-end water also becomes the new highlight. 5100TM Tibet Glacier Mineral Water entered hinterland market with the help of the opening of Qinghai-Tibet Railway in 2006, and it targets at the major cities in North China, East China and South China.

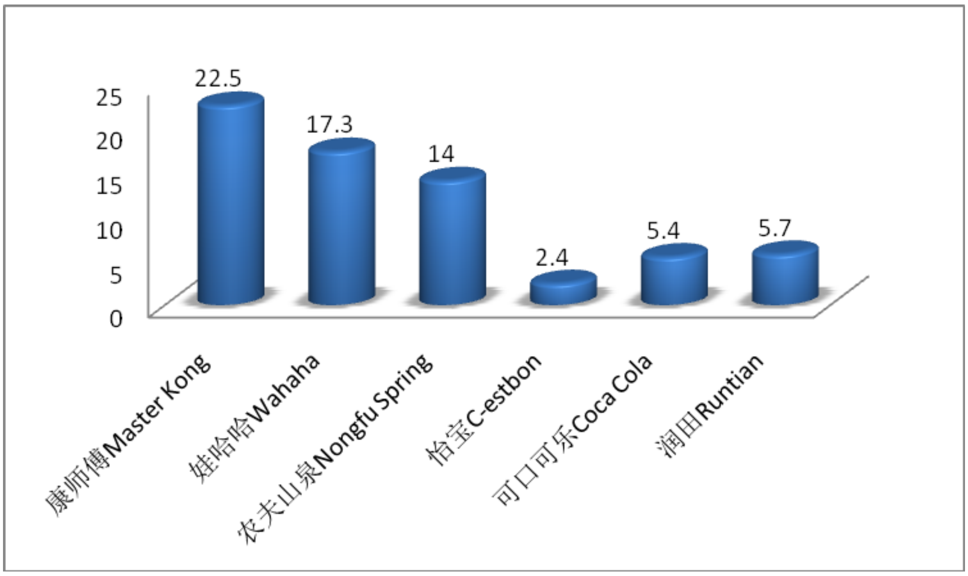
With China’s WTO Accession, the overseas giants also gear their eyes into Chinese market. Danone, for instance, began to march into the bottled water industry after its expansion in Chinese beer industry and dairy product industry. After reorganizing Robust, Danone transfer to target at Wahaha. Also, the European mineral water brand Heidiland enters Chinese mineral water market. With the intervention of foreign capital, Chinese bottled water market will get further integrated.

5. Competition in China Drinking Water Market

5.1Brand Competition

Currently, the three well-known brands, i.e., Master Kong, Wahaha and Nongfu Spring sweep the majority of Chinese drinking water market shares; while Coca Cola, C-estbon and Runtian belong to the second group.

Market Shares of Drinking Water Brands, Sep.2009 (Unit: %)



Source: AC Nielsen, ResearchInChina

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