

中国咖啡市场投资前景调研



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Coffee Market in China: Investing in Chinese Coffee



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摘 要

近年来，中国经济高速增长，已经发展成为仅次于美国的世界第二大经济体。中国消费者的实际购买力已经位居世界第一。在中国市场，咖啡的生产和消费增长正以二位数的速度快速增长，远远超过了咖啡在世界上其他国家的增长速度。

论文从对咖啡在中国种植和生产历史的研究入手，探讨了中国咖啡消费者的特点、市场结构、消费种类、市场占有率及市场增长潜力等方面的问题。目前在中国市场，99%的咖啡仍为速溶咖啡，只有1%为新鲜的现磨咖啡，高质量、高消费的咖啡市场还没有真正形成。但与此同时，咖啡质量正日益受到中国消费者的关注。中国消费者的消费热点正在从原来的只要是咖啡就好，逐步转移为追求更美味、更优质的咖啡。

论文以雀巢咖啡为个案，分析雀巢公司发展历史和在中国的经营模式。目前，中国的各咖啡厂家，包括雀巢咖啡在内，正在将其经营策略从原来的提供快捷便利的咖啡饮品为主，转变到更加关注咖啡原材料（咖啡豆）的种植以及咖啡的制作过程的工艺，以保留咖啡的最佳口味，为消费者提供更加美味的高质量咖啡。

为了掌握中国市场的一手资料，作者实地走访调研了云南咖啡豆种植及投资情况。由于气候原因，云南是中国最适合种植咖啡的地区，中国的咖啡种植也主要集中在这一区域。论文在云南实地调研的基础上，自制了调查问卷，进一步对中国消费者的咖啡消费情况进行定量的问卷调查分析。论文据此对中国未来咖啡市场前景进行了预测，提出了自己的咖啡投资及营销的观点。

本文研究认为，咖啡在中国拥有巨大的市场前景和投资价值。在中国，咖啡不仅有其一般的商品属性和经济价值，而且在社会文化交流中也表现出了重要意义。作为西方文化和现代生活方式的体现，咖啡在中国迅速壮大起来的中产阶级中越来越受到追捧。

中国市场的飞速发展吸引了世界各国众多投资者的目光。本论文的研究有助于世界各地投资者和各咖啡企业了解中国咖啡市场的特点和潜力。文中的论点、论据和结论对咖啡企业和零售商的实际商业运作也具有一定的参考价值。

关键词：咖啡，中国，商业/全球战略，中国顾客，雀巢

ABSTRACT

While although China is still a tea drinking nation, it has also been producing and consuming coffee since the 1990s. This market has been increasing in the double digits while the rest of the world is lucky to see a two or three percent increase each year. The market is dominated by instant coffee with a 99 percent market share. That leaves one percent for the freshly brewed coffee. Nestlé along with other companies have been investing in the coffee production in China to improve the quality of the coffee beans, so that in the future they can use Chinese coffee beans in their products in China and possibly in Asia. This would help them lower costs here and give Chinese coffee a better brand image in the world market eventually.

The Chinese market is a new emerging market and is growing at a very high rate. The coffee market is not the only market that is growing, in general the Chinese economy is doing very well and has become the world's second largest economy in terms of nominal GDP and the largest economy in terms of purchasing power parity. The average incomes are increasing and by 2020 it is estimated that over 54 percent of the population will be part of the middle class. This new emerging middle class will have more purchasing power meaning they will be buying more products as well as want to be perceived socially to be in a higher status. This signifies that this new middle class will follow the trends of Western culture and modernity. Coffee culture is most appealing to the younger generation who are drinking the most coffee as well as the most exposed to the Western lifestyle. Culturally, the Chinese look at things in the long term especially quality. This means that while price may be important, quality is more highly valued. Coffee in China is more of a trend and the consumption is still comparatively low when looking at a nation of this size. However, China is new to coffee and is similar to Japan over 50 years ago when coffee was introduced. Both countries have been following a similar ten-year growth pattern.

This paper consists of nine chapters that look at previous research, the background of coffee, the coffee market in China and Nestlé to get a better understanding of the market. This study also looks at the perception of Chinese coffee to see if this coffee will be well received. An independent study was done that shows whether or not people will buy or drink coffee produced in China, what price it should be, where the quality is ranked compared to other coffee producing countries, and what they taste the participants thought

Chinese coffee would have. Nestlé is already very successful in China, but there is significant room for growth in the brewed products. Nestlé should focus more on this market since the middle class is expected to grow drastically and this market has the most potential. Overall, improving the quality of the coffee beans from Yunnan is suggested if Nestlé wants to use the coffee beans from Yunnan in their brewed products since quality is valued more than the price.

Key words: Coffee, China, Business Strategy, Chinese Consumers, Analysis, and Nestlé

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1 Introduction

1.1 Research Background

1.1.1 Why Coffee?

International Business has numerous different aspects that one can choose from, but International Business is not limited to those aspects. International Business can be applied to almost all aspects of life. Nowadays, with the technology and spread of information, people and products the world is no longer a big place but interconnected through every aspect of life.

Coffee by itself may not seem like a topic for International Business, but in reality, coffee has evolved into a major international market. People usually think of their morning cup of joe as just a drink, but coffee as a product is actually the world's second most traded good after oil (Zhang Nan 2014). Now looking at the fact that most of the Western world lives off the beverage, that leaves the other part of the world that does not. This is very interesting for a few reasons. First, this means that the coffee market is able to expand and that there is potential for substantial market growth which means opportunity. Second, this includes not only the sale of coffee beans and coffee as a beverage but also the production of coffee as well as importing and exporting of coffee. Third, examining the marketing and business strategy of different companies that are expanding or looking to expand in these markets that do not currently have a high consumption of coffee.

One of the biggest markets and with much potential is the Chinese market. China has over 1.3 billion people and that is not including the expat community that grows every year. It is estimated that by 2020 China will have well over 1.4 billion people and has been growing by over five million people every year for the last few years (China Population LIVE). Many companies have tapped into the market potential of China because a market of that size is sure to be very profitable and is consumer driven. Exploring the improvements of coffee production and its economic impact make the coffee market in China a perfect case study. This market is in the beginning stages of the market since China is traditionally a tea drinking country. The market growth is also not limited to simply consumption, but also the growth and production of the coffee beans themselves.

1.2 Literature Review

Johan Wickstrom wrote *Coffee, Country-of-Origin and China* in 2012. He did his research in Kunming, which is the capitol of Yunnan, where the coffee is grown. He thought that people would be more knowledgeable about the product and it would be more likely to find the product in coffee shops, cafes and retailers. Wickstrom interviewed two people who were both local and owned their own company in the coffee business. This was to add more understanding to the quantitative study. He also had a focus group comprised of university students from a Kunming University with different majors. Lastly, he did an online survey to collect research without having to be present.

Wickstrom also asked about what country the participant thought in regard to coffee and his results showed that 26 percent thought of Brazil, 11 percent thought of the US, ten percent thought of Italy, and nine percent thought of Colombia. Surprisingly, nine percent said China which is a higher amount than well-known producing countries such as Vietnam. Another question asked was how quality of coffee from certain countries is perceived.

In his survey, the participants perceived the best quality coffee to be from Italy with an overall mean rating of 7.8 with Brazil coming in second with 7.6 and Colombia coming in third with a 7.3 rating. China actually came in with 5.8 for perceived quality and a 5.6 expected price. The idea behind this was that a perceived quality coffee also has a higher perceived price. The highest expected price was also Italy at 7.4 followed by Brazil at 7.2 and the US coming in third with a 6.6 rating. This also supports that products from developed countries are perceived as having better quality products than developing countries.

The relevant question was asking about the quality of foreign coffee versus coffee from Yunnan. Of the sample size, 44.6 percent of people thought that foreign coffee was better than Yunnan coffee, 5.9 percent thought it was worse than foreign coffee and the other 49.5 percent thought that there wasn't much difference. This sample may be biased on this question as many of the people are from Yunnan and all are living in Kunming. The top reason for visiting a coffee shop was to see friends and the second being to hang out or relax with the third most popular response being to go on a date. 60 percent of respondents didn't ask where the coffee comes from.

His questions regarding instant coffee only apply to 101 of his participants, as these 101 people drink instant coffee. Of the 101 respondents, 55 percent only drink instant coffee once a week or less and ten percent drink instant coffee once every day or more

often. A good number of his participants drink coffee at least fairly regularly and 66 percent said they chose the same brand when buying.

The demographics of his study were a total of 59 percent between the ages of 18 and 27 with another 30 percent between the ages of 28 and 38. Around 44.5 percent were male and 55.5 were female. 51.3 percent were from Yunnan province while 48.7 percent were from another province. Finally, 91.5 percent of his participants were college educated in some way from attending classes and having a Bachelors to having a Master's or PhD.

He concludes that the country coffee comes from does in fact matter to Chinese consumers of coffee. The opinions differ based on different groups of between people. He also states that the big question is how is Chinese coffee perceived by the rest of the world and that it has not received any attention. It is important to find out how coffee from Yunnan will be welcomed in mature coffee markets since more and more coffee is being produced and exported.

Another researcher is Joao Canedo wrote *Delta Cafes- Going to China: Choosing Who to Target and Where to Sell* in 2016. His survey consisted of 83 Chinese nationals between the ages of 18 and 34. Of those, only had 46 people actually drank coffee. The majority of people had a monthly income that was below 14,000 RMB with 70 percent between 3,650 RMB and 10,960 RMB. Of those, the average value of number of cups of coffee per day was 2.30 and an average value price was around 15 RMB. More than 70 percent said that they drank coffee both at home and outside the home. 63 percent said they usually buy coffee at a brand store and 22 percent said coffee shops.

Yang, Hu, Mupandawana, and Liu wrote *Consumer Willingness to Pay for Fair Trade Coffee: A Chinese Case Study* in 2012 that collected data in Wuhan in 2008. Mattingly also used this data for his research. Yang et al. (2012) collected data from 564 respondents in Wuhan in coffee shops as well as outside supermarkets because instant coffee is extremely popular. They wanted to minimize their sample bias by collecting data on different days and did not refer to a specific brand or product. They first asked consumers about consumption habits, then their willingness to pay for coffee, and lastly, basic demographic information.

They found that 68.79 percent of the total consumers bought brewed coffee in the last month, which means that these people are willing to pay for coffee. They also found that 72.5 percent made or brewed one cup coffee or more in the last month which means that they are, in fact, drinking coffee and that 66.23 percent mostly bought brewed coffee

at a coffee shop. This means that coffee shops are growing in popularity. Another interesting result is that 43.95 percent of the participants drink coffee from South America, 26.44 percent coffee from China, and 20.48 percent from Europe. This means that Chinese people like foreign coffee but a good percentage of them also drink coffee from China. This is good for our research. This leads to consumer taste preferences with 41.07 percent drinking coffee with creamer or milk and sugar. It was suggested earlier that Chinese consumers don't like black coffee due to the strong taste. It is also possible, that the market caters to this suggestion and that the Chinese consumers don't know about black coffee. The market consists mostly of instant coffee that already has milk and sugar. The coffee shops that sell coffees such as cappuccinos, café latte, Americano or café mocha also all have milk in them. The mean total ounces consumed per week was 38.91 or about three 12 oz. cups. About a third of the participants of their study reported that they expected their consumption habits to increase over the next year.

The demographics of their study consisted of almost half females and half males as well as 52.1 percent being students and the other percent being employed in management, education or the medical field. This supports the data that white collar and the younger generations are drinking more coffee than the older generations. The mean age was 24 and the mean income per month was 6,000 RMB or 871.71 USD. Lastly, the mean price paid per cup of coffee was 22.09 RMB or 3.21 USD.

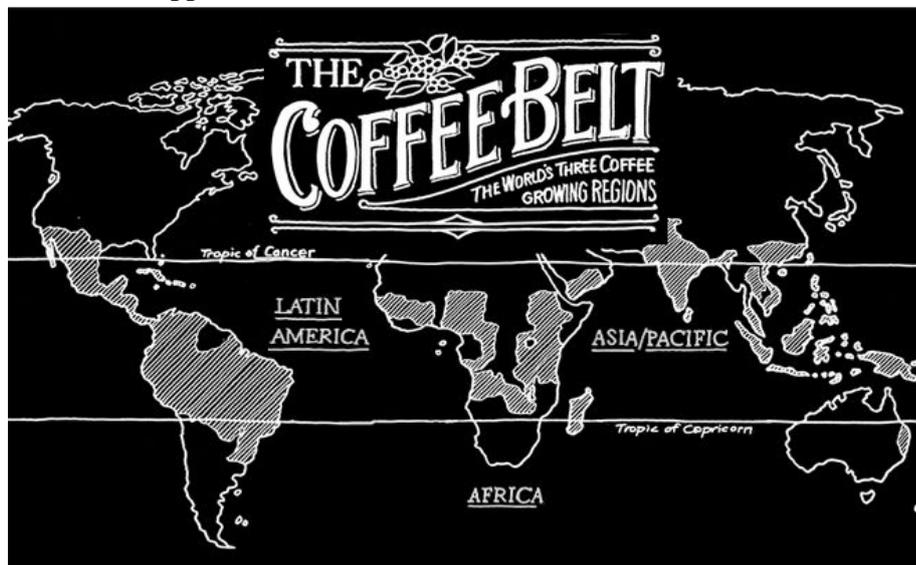
Mattingly (2016) concluded that Chinese consumers placed little to no importance on what the country of origin was for the coffee they consumed. The majority of Chinese consumers are new to drinking coffee and therefore are not inclined towards coffee from any one place. They also cannot discern between good quality and low quality coffee. Chinese coffee drinkers might prefer foreign coffee because it is foreign and presumed to be better quality but it is expensive so they most likely will go with a cheaper domestic brand. As time goes on, Chinese consumers may begin to discern the differences and want a better-quality coffee.

1.3 History of Coffee in China

Coffee is one of most traded commodities in the world second only to oil. It has more than five hundred types and six thousand varieties, most of which are tropical trees or shrubs. Coffee has been around for centuries and was actually discovered by an Ethiopian shepherd in the sixth century. It was introduced in Europe in the 1600's by a merchant of Venice, was planted in the Americas in the 1700's and was in more than 70

countries by the 1920's.

There are a lot of countries that grow coffee. Some of the most well-known are the ones that produce the most amount of coffee each year. The top ten as of 2013 according to the International Coffee Organizations Annual Review are: Brazil with 35 percent, Vietnam with 15.2 percent, Indonesia with 8.8 percent, Colombia with 7.1 percent, Ethiopia with 4.4 percent, India with 3.7 percent, Honduras with 3.1 percent, Peru with 3.1 percent, Mexico with 3 percent and finally Guatemala with 2.6 percent of the world's total production. If you look at the world map you'll see that the coffee growing areas are all on the same latitudes 25 degrees North and 30 degrees South, that has been named the coffee or bean belt near the equator. (Graph: Interesting Facts You Never Knew About Your Coffee, 2016, Appendix 1)



It was initially introduced by a French missionary in the nineteenth century in the Yunnan province of China, which is located in the southwest region of China (See appendix A2). The construction of a railway from Vietnam into China is how the French missionary arrived in Yunnan. The Chinese weren't interested in coffee initially as they have always been a tea drinking country. The production of coffee didn't really become popular until the 1980's when the Chinese government together with the World Bank and the United Nations for Development Programme proposed a project to rejuvenate the area. Nestlé also become involved in the region at that time and as a result the production of coffee took off (ICO 08/10/15, Mattingly 2016).

1.3.1 Chinese Coffee

Coffee is mostly grown in Yunnan province which still accounts for over ninety-five

percent of China's coffee, making a traditionally tea growing region a coffee growing region. Yunnan was known for the Pu'er Tea before it started growing coffee and was recognized for that as well. The Yunnan province is an ideal geographical area for growing Arabica coffee due to the mild climate and mountainous landscape with an elevation averaging around 2000 meters. The region borders Vietnam, Laos and Myanmar which are areas that also grow coffee because of the excellent climate. Arabica coffee needs to grow at high elevations and with such a large area, Yunnan can not only grow coffee but also expand its production. It is important to note that some of this push in coffee production was developed by the drop of tea prices. This led not only tea growers but corn and rice growers to switch to coffee growing because the rate of return was much higher than other crops.

Hainan, a small island located of the southern coast of China, as well as Fujian, a province in the southeast of China also grow coffee (See Appendix A2). They account for the other five percent of the coffee grown in China but they also grow the Robusta type of coffee. Robusta accounts for thirty percent of worlds coffee production. It is easier to care for than other types of beans like Arabica and it also is cheaper to produce with almost double the amount of caffeine.

Over the last twenty or more years, the production of coffee in China has gone from non-existent to being the fourteenth largest producer of coffee as of the year 2015. At the current rate, the area is doubling production every five years and there are no signs of this growth stopping. There have been several large investments by the Coffee Association of Yunnan which has proposed to invest \$480 million or three billion RMB over the next ten years to increase the allocation of land currently farming coffee and the production as well as improve quality, build research centers, and provide training.

Nestlé has also heavily invested in the region and in 2013 provided the funds for a regional coffee center in cooperation with the Pu'er local government. The Pu'er local government also invested ten million RMB to construct a National Key Laboratory of coffee detection. This is the first one in China and provides many services such as industry inspection, research, personnel training, exchanging of foreign technology, and providing technical support for international trade and promoting the development of the Pu'er coffee industry.

Starbucks is also getting involved in the region by starting a program for coffee growers in 2012 and opening a farmer support center, which is only the sixth support center in the world. This support center introduces them to alternative varieties of beans

focusing on improving the quality of beans grown in the region. Starbucks China President Belinda Wong said, “Starbucks Yunnan Coffee Project is about creating a positive change for local China farming communities. We are pleased with the progress of the local adaption tests as it signifies that we are taking one more step forward to completing the Starbucks China value-chain; delivering premium Arabica coffee from bean to cup.” Starbucks also used some Yunnan coffee beans in their *South of the Clouds Blend* in 2009 as well as a second release for the Chinese New Year in 2012. Starbucks told Brand Channel that they look forward to bringing Yunnan coffee to consumers worldwide.

The current quality of the coffee, as the ICO 2015 report suggests, is that the coffee quality isn’t high enough for a specialty coffee label but is too high for solely local consumption. The coffee farmers are also changing from growing mainly the Catimor variety, to growing the Typica and Bourbon variety of Arabica. These types of Arabica have a higher rate of return and are also a higher quality coffee.

1.3.2 Chinese Culture

There are several important things to note regarding the coffee market. Chinese culture puts importance on relationships such as guanxi or the relationship, and values the importance of mianzi or “face” meaning reputation, renqing or favors, and bao or reciprocation.

First, in China hot water dispensers are everywhere. They are in airports, railway stations, workplaces, and in many other locations. The reason behind this is first that people in China drink a lot of tea and second because hot water is important to Chinese culture as in Chinese culture it is said to be good for the body. Instant coffee dominates the market because of this, its price and convenience.

Secondly, Chinese people are very status oriented. Many Chinese drink coffee or frequent Starbucks because it is a status symbol and they can post a picture to show off their stature. This is important because as people in China increase their wealth, they also increase their social and financial status. The western lifestyle, like drinking coffee, becomes something that they want to adopt as a symbol of modernity even if they don’t like coffee they will order something at Starbucks that is tea or a product created for the Chinese market. This ties in with keeping face which is very important in Chinese culture. Keeping face is motivated by the desire to impress others through having luxury goods, showing off their wealth and power to others to achieve a higher social status (Nan, 2014).

Third, China is a tea drinking country. Tea has been a part of Chinese culture for over 4,000 years since the Han Dynasty. Tea was viewed as a special beverage for the royal family at that time and went on to become a drink for everyone in the Tang Dynasty. Not only was tea used as a drink but it was and still is used as a medicine. China has many different teas and even today doctors will prescribe a tea when you are sick. There are teas for sore throats, upset stomachs, headaches and many other things. There is even a great deal of poems, songs, artwork and verses about tea from ancient Chinese intellectuals. This shows the importance of tea culture in China and explains the art of making tea in such a precise way (Yang, 2007).

Fourth, being thrifty was ranked as the top traditional Chinese culture value by the Chinese Culture Connection in 1987. There is value in saving and the Chinese tend to save rather than become in debt. This is starting to change some with people now wanting luxury goods. They are starting to care more about product quality than price. Chinese consumers also value tradition so if they buy a product and it is satisfactory then they are more likely to have brand loyalty and buy products that advertise quality (Nan, 2014).

1.4 Objective and Outline

From an academic point of view, there have been several studies done by other researchers about the Chinese coffee market. Those researchers have focused on trends, consumers, and marketing as well as Starbucks and other companies and their strategies entering the Chinese market. That means it is necessary to examine other aspects of the Chinese coffee market. It is important to relate this to past studies and gain new insights into the coffee market in China.

The objective of this paper is to look at the Chinese coffee market through market research, to get an understanding and examine future prospects of the market. The result will help businesses understand the Chinese coffee market characteristics and potential growth and sustainability as well as assist coffee retailers and businesses. The secondary objective of this paper is to look at Nestle as a case study in the coffee market in Yunnan, research the perception of coffee from Yunnan, and help predict the future of this market. This will relate past studies and gain new insights in the future of the coffee market in China.

This paper will have the remaining sections, in order: Chapter 2 will take a look at the coffee market in China as a whole including a market analysis, the market composition, market growth, and market share by looking at Chinese consumers and

types of coffee as well as provides any relevant regulations and laws in China pertaining to business; Chapter 3 goes into importing of foreign coffee and the exporting of Chinese coffee to understand the market; then Chapter 4 aids our understanding by looking at the case of Nestlé by focusing on their history while also looking at their business strategy; Chapter 5 notes relevant theories; Chapter 6 discusses methodology to the research as well as independent research conducted; and Chapter 7 concludes while discussing future research; and lastly, the acknowledgements, bibliography and appendices follow.

2 The Coffee Market in China

2.1 Market Analysis

It is important to understand Chinese culture to understand the Chinese market for any product. In this case, looking at Hofstede's Cultural Dimensions theory to examine and understand the market as well as a few key factors related to the coffee market.

2.1.1 Hofstede

Hofstede's Cultural Dimensions theory is an analysis of Chinese customers. It is important to understand the culture of a country in order to understand not only the market but consumers buying habits. According to Hofstede the national culture of a country is shaped by the core values it has and defines culture as "the collective programming of the mind that distinguishing the members of one group or category of people from others." Therefore, the culture has a significant impact on the consumer's behavior. The consumption behavior of an individual is developed over time from the culture, the group they socialize with, regional cultures and influenced by family values (Luna & Gupta, 2001). Hofstede's cultural dimensions' theory was created by Geert Hofstede, who worked for IMB at the time, to better understand cross-cultural communication as well as the effects of a society's culture on the value of its members and how they relate to behavior using a structured analysis. There are five cultural dimensions used to analyze a culture (Hofstede, 2001).

The first dimension is Power Distance. Power distance is defined by Hofstede as "the extent to which the less powerful members of organizations and institutions (like the family) accept and expect that power is distributed unequally" China was given an 80 compared to the world average of only 55. If a society has a large power distance like China, then it means that there is an unequal distribution of not only power but wealth. This means that China has a hierarchical structure in terms of power and wealth and that people should respect others with a higher status or rank. The Chinese respect authority so even if one does not agree they follow their superiors (Nan, 2014). In terms of wealth, the classes are divided into upper and lower classes although there is a growing middle class. They are divided by the amount of wealth in each class and culturally there is a divide as well (Hofstede, 2001).

The second is Individualism. It looks into whether a society is an individualistic versus collectivistic society. A higher score indicates an Individualistic society while a

lower number indicates a collectivistic society. China scored 20 compared to the world average of 43. This means China is considered to be a collectivistic society and that it is more group oriented than individual oriented (Canedo, 2016). The Chinese think as a “we” and put high importance on the needs of the group over their own individual needs. This is why the idea of guanxi or relationships is so important to Chinese culture and especially in business. In business if a company has a good relationship with another company whether it be a supplier, a marketer or delivery they will stick with this company because of the relationship (Hofstede, G. H. 2001).

The third is Masculinity. This considers whether a society is more masculine or feminine. Masculine is more assertive and competitive while feminine is more caring and modest. China scored a 66 compared to the world average of 50. This makes China a more masculine society. In China, success and social status are important, as well as wealth and power. The Chinese are very hard working, sometimes working long hours, away from home and their families to have success by achieving a higher salary or a higher position at the company (Nan, 2014).

The fourth is Uncertainty Avoidance with a weak and a strong uncertainty avoidance. Uncertainty avoidance is the degree to which a society prefers rules and structure. China scored a 40 compared to the world average of 64. This makes China a weak uncertainty avoidance society which would mean they are accepting of uncertainty and unstructured situations. In fact, the Chinese need to plan and to have stability. They are open to change and are conforming to new ways of life but they will still place a high value on not losing face or endangering their reputation (Hofstede, 2001).

And lastly is Long-term Orientation. A society can be long term or short term oriented. This study was actually conducted by Chinese Scholars at the Chinese Culture Connection in 1987 and consisted of university students in 22 countries. This factor determines a society's perspective on time and how to deal with difficulty in life. It was initially created by Michael Harris Bond and was based on Confucianism with a strong relation to recent economic growth.

Hofstede got permission to add it as his fifth dimension. China scored a 118 with a world average of 48. This is actually the highest-ranking country. China is a long-term oriented society with values like perseverance, thrift, ordering relationships by status, and having a sense of shame. This make sense since China has been around for centuries and is still going strong. Chinese people and Chinese culture value traditions as well as the past. They look to the future with persistence and the pursuit of goals. Many people in

China will invest or save money their whole life and then when they are older spend the money on a house or something of this nature instead of buying things that they might want now for instant gratification (Wang et al, 2014). In terms of marketing this is good for companies that use durability and quality as slogans suggesting that their products will last a long time (Canedo, 2016). In terms of doing business this means that it can take longer to do business and foreign companies must be patient (Hofstede, 2001).

2.2 Market composition

The coffee market in China is consisted of instant coffee such as Nestlé, ground coffee and freshly brewed coffee in coffee shops such as Starbucks, Maan Coffee, and Costa Coffee. Starbucks being the most well-known coffee shop in China and has a majority market share. In 2013, Starbucks had a 31.5 percent market share in China with UBC at 22.5 percent according to Euromonitor International. China is still a predominantly tea drinking country with sales of tea to coffee being ten to one. Nestlé was the first multinational to enter the Chinese coffee market and has the largest share of the instant coffee market. Some people might even refer to saying the word Nescafe instead of coffee.

2.2.1 Chinese consumers

It is no surprise that larger cities such as Shanghai and Beijing have a higher consumption of coffee due to the sheer size and number of people but also the exposure to Western culture and demand from foreigners. The demand is spreading from these first-tier cities to second tier and possibly even third tier cities.

Expatriates make up a large number of the coffee consumers in China. Expatriates have more knowledge about coffee and are most likely used to drinking coffee on a regular basis therefore would frequent coffeehouse more than Chinese nationals. In the 2000s 30 percent of customers at coffeehouses like Starbucks were Westerners, businessman from Hong Kong and Taiwan. Reports from Shanghai shows that around 230,000 Taiwanese go to Shanghai for a period of a few months and that this group of people increase the coffee consumption (Nan, 2014).

Another category would be Chinese nationals returning from overseas studying, working or travel. They were exposed to coffee while abroad and either liked the flavor or liked the atmosphere and lifestyle. These returning Chinese continue to go to coffeehouses and buy coffee. There is another category that is relatively small that consists of people, Chinese or foreign, that don't like coffee but enjoy the atmosphere or

the Western products (Nan, 2014).

2.2.2 Ground vs Instant

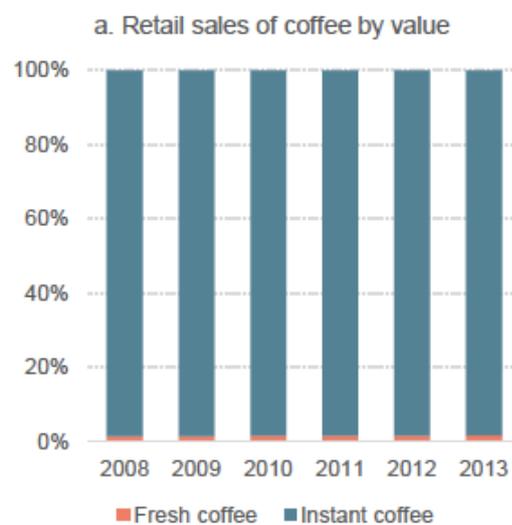
Since Nestlé entered the market first and coffee was an unknown to the Chinese people and the market, it is no surprise that the foreign companies Nestlé and Guangzhou Kraft are the major sellers of instant coffee. This is the same for the fresh coffee market as well with Starbucks being the one of the first to enter the Chinese market followed later on by other companies such as Maan Coffee and Costa Coffee. These companies also dominate the fresh coffee market, with Starbucks being the most well-known. This shows us that the Chinese coffee market is completely run by international brands. There are a few domestic instant coffee makers but they account for less than one percent of the market. It was mentioned earlier that the Chinese also like Western culture and lifestyles, so many Chinese believe that foreign brands are of better quality and have a better reputation.

Nestlé is in a unique position because the company is an international company based in Switzerland so that gives it the foreign name and assumed better quality while also being domestic and using local supply. This makes it both a foreign and domestic brand in a way. Nestlé coffee also comes from Yunnan, which grows a world known tea of high quality, so this gives the domestic Nestlé product a perceived better quality.

Instant coffee has around 99 percent of the retail sales volume and 98 percent by value of the coffee market in China (Postma, E., et al). The amount of coffee shops is growing in China and more and more people are drinking coffee, especially the younger generations. Instant coffee can be found in most work places and is thought of as an afternoon pick me up to keep employees awake (Graph: Coffee in China, 2017, Appendix A3).

You can buy a Nescafe 2+1 box of 43 coffee with milk instant coffee packs for 49.80 RMB or 7.22 USD. You can also buy a Nescafe box of 20 black instant coffee for 14.60 RMB or 2.12 USD. You can buy these kinds of instant coffees at almost every convenient store as well as grocery stores like Walmart, where the price was taken from in

Figure 1: Market composition of retail sales by value



Source: Euromonitor International

March 2017. There are several different types including black coffee, coffee with milk, or coffee with milk and sugar. This is very cheap per cup of instant coffee and with almost every place you go having hot water you can have coffee anytime, anywhere, any way.

As of 2009, Nestlé's Nescafe had 68 percent of the instant coffee market with Guangzhou Kraft's Maxwell House following way behind at 14 percent and the other companies all having 1 percent or less. The data from 2009, also shows that Nestlé and Guangzhou Kraft combined account for more than 80 percent of the total retail value sales. According to Euromonitor International's report in February of 2017, Nestlé continues to dominate coffee in China with every two out of three cups of coffee being Nescafe and a 66 percent retail value share in 2016. Nestlé maintains its market share due to several factors including entering the Chinese coffee market when China first opened its economy, its range of both instant and brewed coffee products, and recently Maxwell House saw a drop-in sales, Nestlé's biggest competitor in China. There was a three percent increase in retail volume sales in 2016 due to rising interest in coffee (Coffee in China, 2017). Nescafe in 2012 was the number one liked brand among Chinese young adults ages 16 to 24 and was selected as the "most loved brand" by Chinese university students from 2006 to 2011 (Schipper, H., 2012).

Ground coffee on the other hand, has a huge market potential especially if it only has one percent of retail sales and two percent value. First, the middle class is growing and so more people have more disposable income. According to a study done by McKinsey & Company 76 percent of China's urban population will be part of the middle class by 2022. The study also says that these households will be earning between 9,000 to 34,000 USD a year. This is a drastic increase from 2000 when the urban middle class was only around four percent. As of 2015, the urban population was around 730 million people and is expected to grow, meaning that by 2022 over 550 million people will be considered middle class. McKinsey & Company write that that would make China's middle class large enough to be the third most populated country in the world (Barton, D. et al 2013). This new middle class want a better lifestyle and are looking for better products. Second, when people are outside their homes and workplace they are going to coffeehouses because they not only want to drink fresh coffee but they don't have coffee makers at home in the first place so they can't make fresh coffee at home. Third, instant coffee accounts for 90 percent of consumption of coffee which leaves fresh coffee ten percent and much room for growth. It may be harder to grow this market because it is still relatively expensive compared to western countries and also instant coffee. A medium

latte at Starbucks cost 33 RMB or 4.79 USD, using a conversion rate in March 2017. This is significantly higher than the box of Nescafe you can buy at Walmart.

It should be noted that Nestlé not only has the Nescafe instant coffee packs but also brewed coffee as well. This brewed coffee comes in the form of Dulce Gusto, an individual cup of brewed coffee maker and Nespresso which is their high-end coffee maker. This type of coffee hasn't really gained much market share due to the ease and convenience of instant and freshly brewed coffee from coffee shops. In fact, in the grocery stores one cannot even buy this type of coffee. The only coffee available is the instant coffee packs and instant coffee by itself.

2.3 Market Growth

Since China was traditionally a tea drinking country, the cities with the highest consumption are the cities that have the biggest populations and a higher percentage of expatriates. Since the coffee market is still in the beginning stages the major cities were the first to be introduced to coffee culture. The capital Beijing along with Shanghai and Guangzhou have the highest consumption. These cities are the most international cities in China as well as many Chinese consumers being more exposed to the Western lifestyles and following those trends. This Western lifestyle is appealing to the young, affluent and urban consumers by drinking coffee a beverage as well as a social status. First, if a person can afford a cup of brewed coffee then they have some money and at least are not in the lower class. Second, drinking a cup of coffee shows that a person is open and adapting to a Western lifestyle (The Coffee Industry in China, 2016).

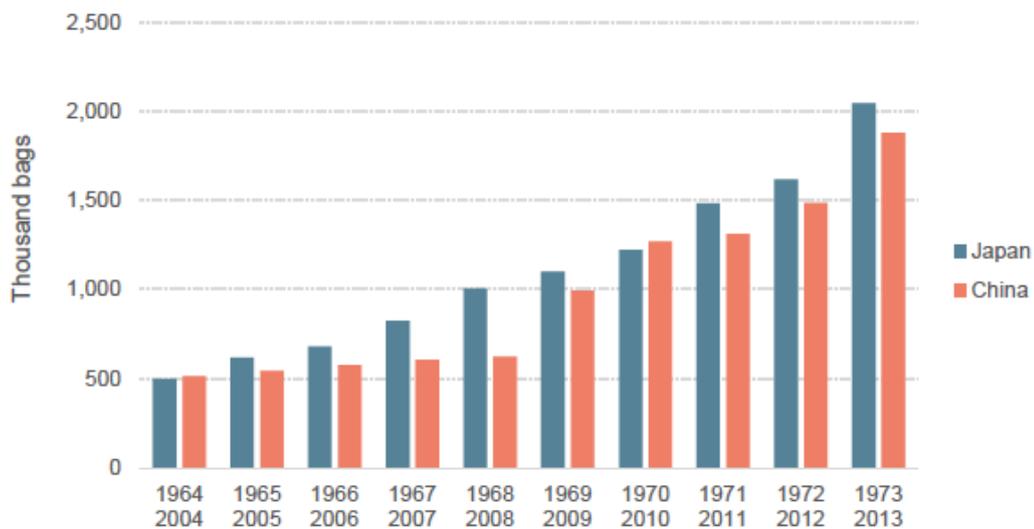
In terms of annual consumption, China has gone from consuming 199,000 bags of coffee in 1998 to 1.2 million bags in 2012. This gives the market an annual growth rate of 12.8 percent which is very high compared to the international growth rate at 2-3 percent (ICO, 2013). According to the ICO if that growth rate continues, China will reach a consumption of 2.8 million bags by 2020. With there being so little of the market drinking coffee whether it be instant, ground, or freshly brewed there is a large market to be gained. According to a Nestlé report in September 2012, China was only three cups of coffee per capita compared to even Hong Kong at 168 cups per capita or the US with 451 cups per capita (Schipper, H., 2012).

The boom of online shopping in China is not limited to any one industry. Online shopping is almost bigger than in store shopping due to the convenience. Coffee is also being sold online on platforms like Taobao and Amazon. In 2009, the amount of coffee

bought online increased 60 percent from 2008. In 2010, the amount increased 113 percent from 2009 and increased 112 percent in 2011. As you can see this online market is growing rapidly as well with the instant and ground coffee markets growth.

China is being compared to Japan over 50 years ago. Japan like China has always been a tea drinking nation. In the 1960s coffee was introduced in Japan and steadily grew into one of the largest coffee markets in the world. In the 2000s it was consuming over seven million bags of coffee making it the fourth largest coffee consumer in the world. It took almost 40 years for Japan to become this coffee powerhouse. China is from 2004 to 2014 is being compared to Japan 1964 to 1974. During this ten-year time frame the coffee consumption of both countries has grown at similar rates. China is still in the early stages of this market development, but if it continues and follows the same path as Japan, China will surpass the U.S. and Brazil to be the world’s largest consumer of coffee (ICO, 2015) (Graph: ICO, 2013, Appendix A4).

Figure 5: Coffee consumption in China (2004/05 to 2013/14) compared to Japan (1964/65 to 1973/74)



2.4 Competitive Advantages

The Chinese coffee market has three competitive advantages right now. The first, is that 90 percent of the coffee trees are the Catimor variety which is resistant to coffee leaf rust. This means that more of the trees will produce good cherries and less loss. The second, is that there are no nematodes which are a micro-worm that infests the roots of the trees and the tree then dies. This also signifies that there will be less losses in terms trees and the amount of cherries they produce. Lastly, the third advantage is that there is no coffee berry borer which are a kind of beetle that eats its way into the cheery and lays

eggs. The beetles then hatch and eat the coffee beans. While although there are none in Yunnan yet, there are said to be coffee berry borers in Myanmar and Vietnam, which are located on the border with the Xishuangbanna region that borders Pu'er. Both Xishuangbanna and Pu'er are located in the Yunnan province but Xishuangbanna is further south than Pu'er. So, while the beetles have yet to reach the region, it is possible that they will eventually reach Pu'er given the relatively short distance from Vietnam and Myanmar.

2.5 FDI Regulations

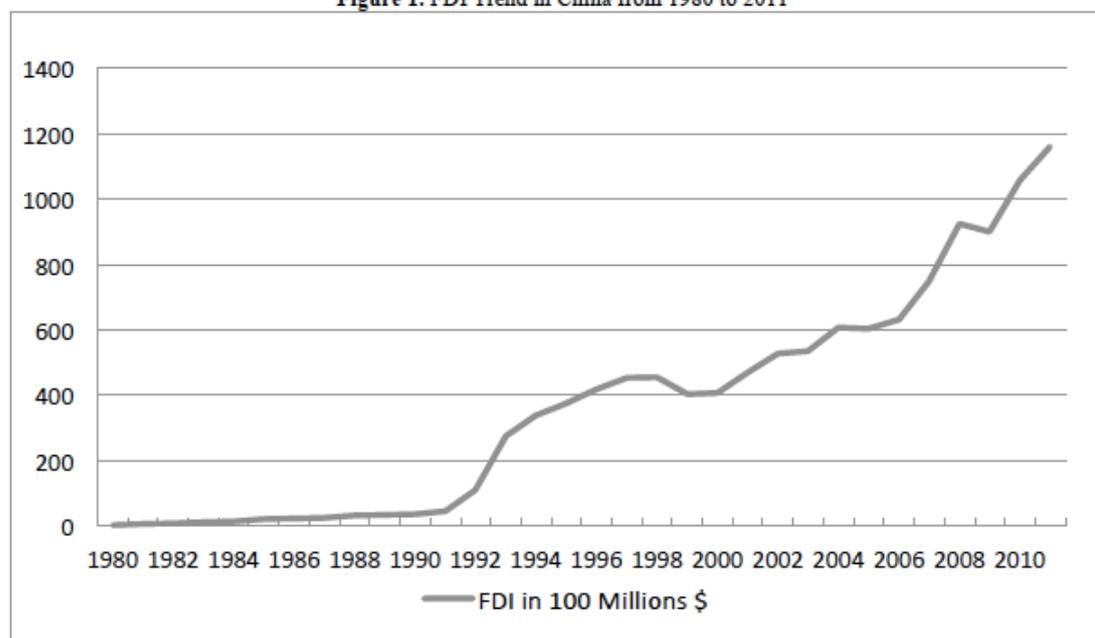
The first law regarding foreign direct investment was the "Law of the People's Republic of China on Joint Ventures Using Chinese and Foreign Investment" in 1979. This was when China opened its economy to the outside world. In the 1980s the government establish five special economic zones that were on the coast from Shenzhen, Zhuhai, and Shantou to Xiamen and Hainan that were set up to encourage foreign trade and investment. These economic zones had the advantages of lower income and land-use taxes, a more simplified administrative procedure and tariff-free imports of certain products and supplies.

From 1984 to 1986 other coastal cities were opened up for investment like the special economic zones but were called coastal open cities. They were Fujian, Guangdong, Guangxi, Hebei, Jiangsu, Liaoning, Shandong, Shanghai, Tianjin, and Zhejiang. These coastal cities were part of the preferential policies. At that time, the Ministry of Commerce of China out great importance to improving the investment environment and maintaining policies to develop high tech industries and focused on industrial products that that the economy would be developed at a fast and steady rate. These coastal cities also allocated some land called an Economic and Technological Development Zone. The coastal areas had a very high rate of success and improved the economy with over 160 million people affected by this change.

Since this was so successful, China also opened up and promoted the development of other areas in China such as the central and western regions. This led to the creation of 27 Economic and Technological Development Zones in central and western China and in 2007 there were five special economic zones, 14 coastal open cities, 54 national Economic and Technological Development Zones, 15 free trade zones, 53 high technology industrial development zones and 38 export processing zones. All these zones have transformed China from a closed economy to an open economy that has gone from

small cities with farmers to megacities with billions of people and into one of the world's largest economy. As of 2015, China received the largest amount of FDI out of developing countries and was only second to the US worldwide. Prior to the 1990s there was little to no FDI in China due to China not being open for FDI until 1979. From 1990 to 1999 China saw a drastic increase of FDI with around 4.3 billion dollars in 1991, 11.2 billion in 1992 and 25.7 billion in 1993. That's a growth rate of over 130 percent in one year. According to the National Bureau of Statistics of China from 2000 to 2010 there was a steady increase in the amount of inward FDI in China, in constant dollars, was 40.7 billion USD in 2000, 114.7 billion USD in 2010 and 123.9 billion USD in 2013. The United Nations Conference on Trade and Development or UNCTAD shows that more recently that in 2013 inward FDI was 123.9 billion USD with an increase of 3.7 percent in 2014 to 128.5 billion USD and up 5.5 percent in 2015 to 135.6 billion USD (Wei, S. J. 1996) (Liang, Y. 2015) (Graph: China Statistical Yearbook, 2015, Appendix A5).

Figure 1. FDI Trend in China from 1980 to 2011



Source: China Statistical Yearbook by China's National Bureau of Statistics

FDI has played a significant role in the Chinese economy and its success. In the 1980s most of the FDI was invested in the primary sector that consists of agriculture, mining and petroleum with 40 percent of the total invested in these areas. The secondary sector consists of manufacturing and the tertiary sector of construction and transportation, wholesale, and the retail and service industry. The secondary sector received 27 percent of the total investments while the tertiary received 32.1 percent. In the 1990s it changed drastically with the primary sector only receiving 3.1 percent while the secondary

received 51.2 percent and the tertiary 47.3 percent. The tertiary sector at that time was mainly FDI into real estate. From 1995 to 2005 the accumulated FDI investment into the primary sector dropped to 2.3 percent while the secondary rose to 69.6 percent and the tertiary dropped to 28.1 percent (Sharma, et al 2014).

FDI is also very unevenly distributed geographically in China. In the beginning when FDI was first allowed, the eastern and coastal regions were the first to be opened up and allow FDI. Naturally in the 1980s eastern China received 88.9 percent of the inward FDI leaving the other 11.1 percent to central and western China combined. Soon after the government wanted to promote the central and western parts of China for development so by 1997 these areas had rose to 17 percent of the FDI and by 2008 was up to 22 percent. The eastern part of China was the first to receive investments and therefore has developed significantly over the years becoming some of the biggest centers of trade and investment in the world. The eastern and central parts of China are still a priority in China (Sharma, et al 2014).

A good example of this is Chongqing, which is located in central China and was once part of Sichuan province and is now its own municipality. Chongqing 30 years ago was little more than a small city that heavily relied on farming and fishing in the Yangtze and Jialing rivers with the confluence at the city center. Today, Chongqing is a city that has completely transformed with around nine million people in the city and a total municipal population of over 34 million. Chongqing has been one of the fastest growing cities in China and in the world. Chongqing greatly benefited from the government campaign to “Go West” that aimed to develop central and western China with business and investments and is a good example. Chongqing is now home to Fortune 500 companies such as Ford and Microsoft and has more than quadrupled its GDP since 1998.

These FDI regulations are important for companies such as Nestlé since it first invested in dairy in Shuangcheng, Harbin part of the Heilongjiang Province in the northeast part of China in 1986. At that time, Nestlé negotiated with the government to enter China and entered as a joint venture. While although all of Nestlé's investments are important, and have contributed to the economy, this region wasn't part of any of the zones that were initially set up to receive investments. Nestlé also invested in Yunnan a southern region of China, this was due to the fact that coffee was well suited for growing in this region. It should be noted that Nestlé tried to invest in Guangdong, and eventually did, which is one of the special economic zones and since the government required a local supply chain Nestlé also invested in Yunnan. This correlates with the distribution of FDI

in the 1980s into agriculture. Nestlé was trying to take advantage of these zones and the advantage they offered. Over the years since Nestlé entered the Chinese market they have expanded to Beijing, Shanghai, Xiamen and Hong Kong. Shanghai was set up as a coastal open city but given its location has gone on to become one of the most important cities for the economy as a hub for not only importing, exporting and as an industrial base, but is also one of the biggest financial and trade centers in China. Xiamen was set up a special economic zone, whereas Beijing is the head of the government and Hong Kong has gone on to become a main world hub of economic trade and business as well as a major manufacturer. Nestlé has strategically invested and developed in areas that are on the eastern or coastal areas of China to make use of the location and access to guarantee their future. Previous research by Cheng and Kwan (2002) says that foreign investors “tend to invest in regions where there is already a high concentration of foreign firms, which is also an indication of the positive role large market size, good infrastructure and preferential policy have on FDI stock.” This is true for cities like Shanghai, Hong Kong and Beijing where foreign companies have flocked because these cities are not only the three most important cities in China, but also have become international centers for business and finance as well as entrepreneurship. Nestlé chose these cities for their offices and factories to have the advantages of being located there and started their dairy and coffee projects in other areas to aid development in these underdeveloped areas with guidance and approval from the government (Liang, Y. 2015).

3 Imports vs Exports

3.1 Importing

China didn't import coffee until the 1980's and afterwards was mainly importing coffee because the amount of coffee grown and produced in Yunnan and the surrounding regions was so low. As of 2014, China had imported around 1.4 million bags of coffee which is significantly higher than 2005 when it only imported 418,000 bags. China has been increasing its imports of coffee at an average annual rate of 15 percent each year over the last ten years.

There are three main distribution centers in China for coffee beans that are imported. They are situated in Beijing, Shanghai, and Guangzhou. These are the three largest cities in China. Guangzhou is located in the south of China near Hong Kong and processes the imports from Southeast Asia like Vietnam and Indonesia. Shanghai is the largest of the three distribution centers and is located in the East of China on the coast. Shanghai accounts for more than 50 percent of the total coffee imports. It has an excellent location being one of the most international cities in China while also having a major port. The final and most important center is Beijing. There is no doubt that this northern city in China has the largest amount of coffee consumption being that it is the ruling city of China and therefore all major foreign governments and companies are based there.

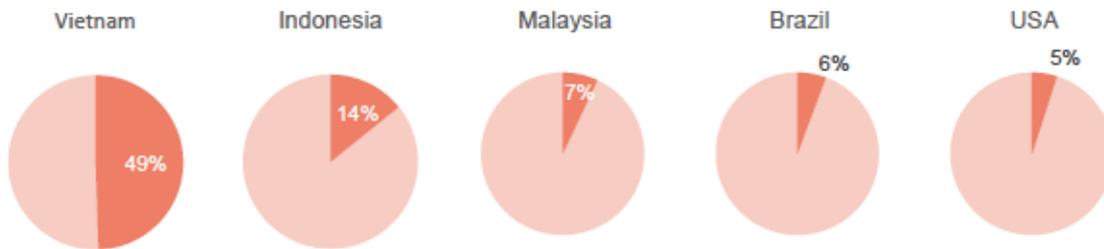
There are three types of imported coffee: green coffee, roasted coffee and soluble coffee. The coffee imported is mostly green coffee that is unprocessed and is most likely since it has a lower price and can easily have many different uses. This accounts for an average of 69 percent of the imports from 2010 to 2015. In 1998 China imported 140,000 bags of green coffee while in 2012 it imported 985,000 bags. The demand for soluble coffee is increasing at a rapid rate with the national demand for these products growing faster than the domestic markets processing capacity.

3.1.1 Where importing coffee from

China imports almost half of its coffee from Vietnam which makes sense since Vietnam and China share a border. Chinese coffee drinkers don't like pure Vietnamese coffee because of the strong taste so instead it is mixed with coffee from Yunnan. (Nan, 2014) After Vietnam, Indonesia accounts for around 14 percent of the imports, Malaysia seven percent, Brazil six percent and the USA five percent of the total imports. The top three countries China imports coffee from are relatively close and this not only makes it

more convenient but also a quicker delivery. Brazil and the US are further away and would automatically take longer to arrive in China. Coffee from Brazil and the US would most likely be more expensive as well (Graph: ICO 2015, Appendix A6).

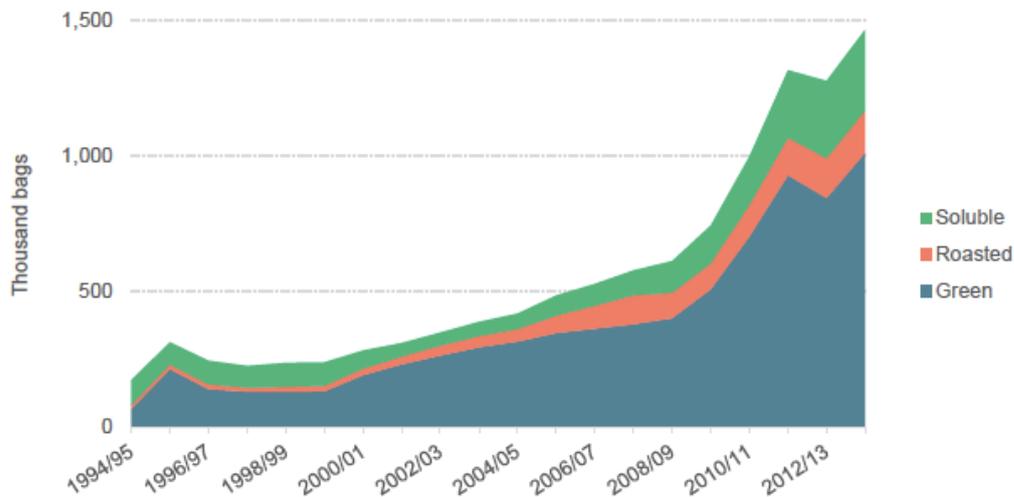
Figure 4: Origin of coffee imports by China (Average: 2009/10 to 2013/14)



3.1.2 Quantity

As the graph illustrates, there was a steady increase from 2000 to 2007. It also shows that from 2008 to 2011 there was a sharp increase in the imports with an increase of 21.4 percent from 2008 to 2009, 34.09 percent from 2009 to 2010 and 32.06 percent from 2010 to 2011. This shows that the market demand is higher than the amount coffee producers can produce. Production also increased in this time, however some coffee was also exported (Graph: ICO 2015, Appendix A7).

Figure 3: Coffee imports by China by form of coffee



3.2 Exporting

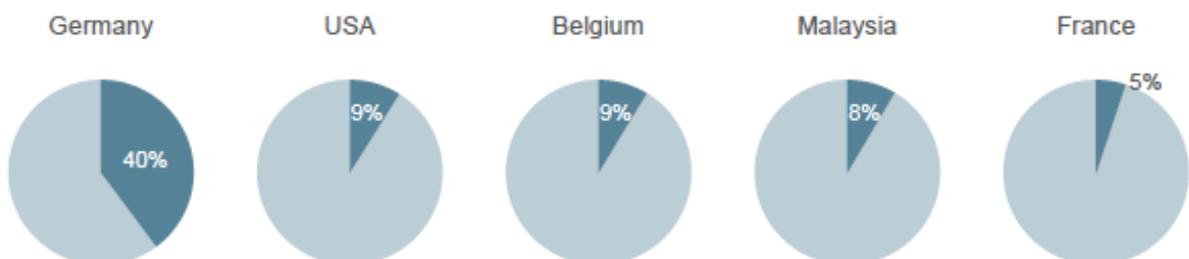
China's coffee exports have been following the increase in production. Over the last 20 years, China went from exporting only 58,000 bags of coffee in 1994 to exporting over 1.2 million bags in 2014. That's almost a two-thousand percent increase at 1,968 percent higher. China mostly exports unprocessed, green coffee beans with 90 percent of the exports being these unprocessed beans and an average of four percent being soluble products or for the instant coffee market.

It is interesting to note that in 2009 there was significant increase in exporting by about 51 percent from 2008. This is supposed to be due to an agreement signed by Yunnan Dehong Hood Co., Ltd and ECOM Coffee Group based out of Switzerland. This agreement stated that the Chinese company would export 240 tons of coffee per month and has greatly increased the amount of exports.

3.2.1 Where exporting coffee to

China exports the majority of its coffee to Germany. Germany accounts for 40 percent of the total exports. The USA comes in second with nine percent, Belgium also at nine percent, Malaysia at eight percent, and France at five percent. China does export coffee to over 90 different countries. It is interesting to note here that China imports seven percent of its coffee from Malaysia but then exports eight percent back to Malaysia as well as the USA exporting five percent of China's coffee and then importing nine percent. Many times, with unprocessed, green coffee, the coffee is processed and re-exported to be used in products (Graph: ICO 2015, Appendix A8).

Figure 8: Destination of coffee exports by China (Average 2009/10 to 2013/14)

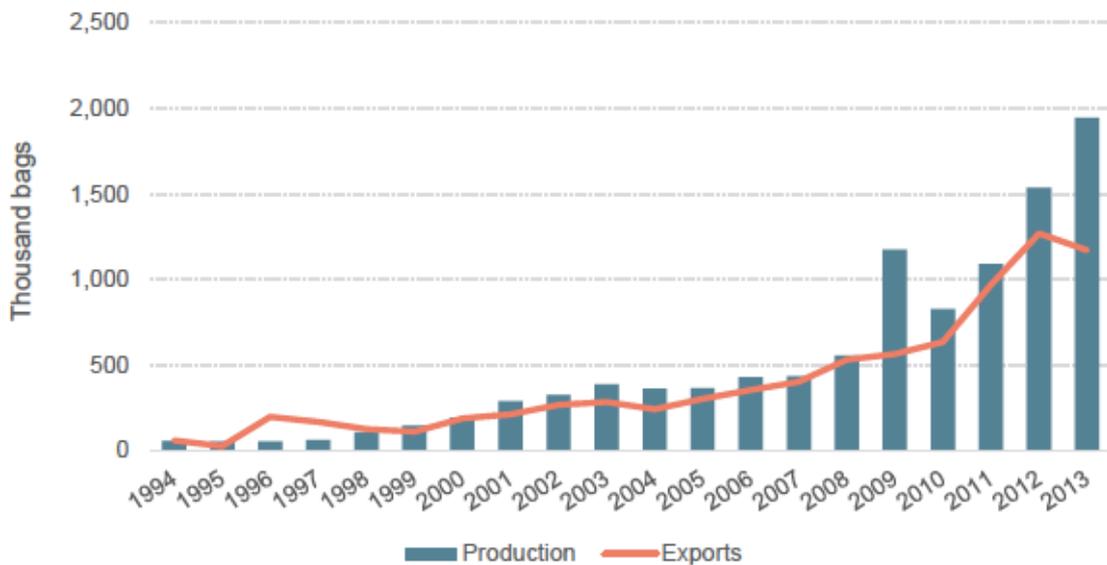


3.2.2 Quantity

As the graph illustrates, from 1999 to 2013 exports were equal to or greater than production. Exports showed the greatest increase change from 2010 to 2011 at 53.08 percent and 2011 to 2012 at 30.0 percent increase. As production increased so did exports

(Graph: ICO 2015, Appendix A9).

Figure 7: Production and exports in China (1994/95 to 2013/14)



3.2.3 Expansion

There is room for expansion in this market. China is increasing its production with many companies and the Yunnan local government investing in the coffee growing and production. Every year the market is growing in the double digits. From 2004 to 2013 exports increased on average 19 percent while imports from 2003 to 2013 increased an average of 15 percent. Production also increased on average of 21 percent. The demand for coffee domestically is higher than what the farmers can produce, therefore if the farmers can produce more they can supply the domestic market. One of the main focuses is to improve the overall quality of the beans which will help the farmers if they produce more in the future. Additionally, if the farmers produce enough to supply the domestic market, then it is possible for them to produce enough to also supply the companies that want to sell internationally.

4 Discussion: The case of Nestlé

4.1 Background

Nestlé was founded in 1866 by Henri Nestlé who was a pharmacist and developed a milk-based baby formula. It was founded as the Anglo-Swiss Condensed Milk Co the next year in 1867. The company launched cereal and in 1904 added chocolate to its products by signing an agreement with Swiss General Chocolate Company. Then in 1905 the company merged with the Anglo-Swiss Condensed Milk Company and became known as Nestlé.

The last seven years have seen many changes in Nestlé related to coffee and in China. In 2011, Nestlé formed a partnership with Yinlu Foods Group, a Chinese food company as well as acquired a 60 percent stake in Yinlu. In 2012, it launched Nescafe Alegria, a new coffee machine for small business in Europe. Nestlé launched Nescafe Dolce Gusto in Australia and two research and development centers in Xiamen and Dongguan, China.

In 2013, Nestlé opened a new research and development extension in Singapore along with opening its first Nespresso store in San Francisco in the US and in Tokyo, Japan. The company announced its plans to invest 44 million euros on new technology for its Nescafe factory in Girona in north-eastern Spain and established a factory in Vietnam, and a coffee center in the Philippines.

In 2014, Nestlé opened its latest Chinese research and development center for confectionery and ice cream in Dongguan, China. Nestlé initiated a new Nespresso sustainability strategy through 2020 based on a 500 million CHF investment called the Positive Cup. Nestlé also opened a new coffee factory in Schwerin, Germany to increase production capacity of Nescafe Dolce Gusto. Nestlé started a joint venture with Lotte Foods and formed Lotte- Nestlé Korea to make and distribute Nescafe Coffees, powdered chocolate and other beverages in Korea. The company launched Nespresso Vertuo Line, a new large cup system in the US and Canada. Nestlé also established a Nestlé Food Safety Institute research center in Beijing. Nespresso, a Nestlé subsidiary, opened commercial operation in Colombia as well as Nestlé announced its plans to invest 1 billion US dollars in Mexico to build two new factories which is the company's sixth largest global market (Canadean Nestlé S.A.).

The company has an extensive history that has not been detailed as the company has had significant acquisitions, but now can clarify what products and brands Nestlé actually

sells. From the history and information earlier in the paper it is known that Nestlé sells coffee under Nescafé and Nespresso as well as other coffee products but they also sell coffee creamer called Coffee-mate. Nestlé sells everything from baby foods, bottled water, cereals, chocolate and confectionary, chilled and frozen foods, and dairy to drinks, food service, health-care nutrition, ice-cream, pet-care and weight management.

Nestlé sells baby foods under the brands of Cerelac, Gerber and Gerber Graduates, NaturNes, and Nestum. Nestlé sells bottled water under the brands Nestlé Pure Life, Perrier, Poland Springs, and S. Pellegrino. It sells cereal under Chocapic, Cini minis, Cookie Crisp, Estelitas, Fitness, and Nesquik Cereal. Chocolates and Confectioneries are sold under Aero, Butterfinger, Cailler, Crunch, Kit Kat, Orion, Smarties, and Wonka. Nestlé sells culinary, chilled and frozen foods under Buitoni, Digiorno, Herta, Hot Pockets, Jack's, Lean Cuisine, Maggi, Thomy, and Stouffer's. Nestlé dairy brands include Carnation, Coffee-mate, La Laitere, and Nido. They sell drinks under Juicy Juice, Milo, Nesquik, Eggstra, Nestea and Boost. Nestlé ice cream brands are Dreyer's. Extremem, Haagen-Dazs, Movenpick and Nestlé Ice cream. And lastly Nestlé sells pet care under Alpo, Bakers Complete, Beneful, Cat Chow, Chef Michael's as well as weight management under Optifast.

4.2 History in China

Nestlé was one of the first multinational companies to enter China and was the first to establish a coffee processing plant. It initially started in 1874 when the company started trading in Hong Kong. Then in 1908 it opened an office in Shanghai. In 1920, Nestlé Products Ltd. was set up in Hong Kong. From the 1920s till the 1980s China's economy was not open for business. Nestlé did however talk with government officials concerning partnerships in China near 1980.

Nestlé entered the Chinese market as a joint venture with Shuangcheng, a state-owned enterprise in the north of China in 1986. Heilongjiang province where Shuangcheng is located, was the opposite of the areas like Shanghai and Shenzhen where trade and manufacturing were rapidly growing. There they built a factory in 1990 and helped the local farmers by setting up infrastructure and paying them at the time of purchase for the milk. They had Swiss experts help the farmers since Nestlé then had over 100 years' experience producing milk and infant nutrition. The experts helped the farmers in practices for caring for the cows and later went on to train them on better techniques and technologies. They worked closely with the government and it was a win-win

situation for all parties involved. Nestlé has helped produce local products made by local farmers and ingredients of high quality so that China doesn't need to import and it saves on foreign exchanges.

Nestlé Dongguan was also another joint venture in 1991 with another state-owned enterprise, not mentioned, where they were allowed to set up another factory to manufacture Nescafe products. The government also asked that Nestlé help the locals and set up a supply chain. In 1992, Nestlé set up an agricultural assistance service center as well as an experimental and demonstration farm in 1997. At that time, Nestlé had invested over 20 million RMB in Yunnan.

In 1992, Nestlé set up a factory in Hong Kong to produce dairy and ice cream by acquiring a dairy farm. In 1996, Nestlé China Ltd. established a headquarters based in Beijing and is a subsidiary to Nestlé S.A. headquartered in Switzerland. They also established a partnership with *Totale* in 1999 where they owned eighty percent interest. By 2001, the company had a research and development center in Shanghai and in 2002 established another partnership with *Haoji* where they owned an eighty percent interest. By 2008, the company had opened another research and development center in Beijing and in 2009 opened a second *Totale* factory in Shanghai which became the world's largest bouillon factory. In 2010, Nestlé took control of seventy percent interest of the partnership with *Dashan* and in 2011 took sixty percent interest of in partnership with *Hsu Fu Chi* as well as sixty percent control of the partnership with *Yinlu* Foods Group.

As of 2015, Nestlé had over 330,000 employees in 197 countries with a value over 200 billion US dollars. Nestlé has a market cap as of December 2016 of over 222 billion which was calculated taking the price per share times the number of outstanding shares. In December of 2016 it was 71.74 USD per share with 3.098 billion shares which equals 222,248,000,000. As of April 2017, the market cap for Nestlé is over 231 billion with outstanding shares at 3.112 billion and 74.50 USD price per share. In China, Nestlé sells over 35 million products daily and China is the second largest market for Nestlé. Over 95 percent of Nestlé products that are sold in China are produced and manufactured locally. Nestlé as a company has diversified themselves so that the company has products for everyone no matter what class from the poor to the upper class to global aficionados from dairy to coffee and beverages, water and cereals to pet foods. Nestlé also adapts its products and partners with local companies to change to the countries tastes and preferences.

4.2.1 Nescafe in China

Nestlé was the first multinational company to enter the coffee market in China and has since become a household name for coffee in China. The instant coffee shelves in the supermarkets are monopolized by Nestlé Nescafé. Nestlé first started out in China's coffee market in 1988. At that time, Nestlé wanted to set up a Nescafe processing center in Guangdong Province. They were interested in doing this because they were growing in the Chinese market. The Chinese government said that if they wanted to set up a processing center they needed to set up or open a supply chain. Initially, Nestlé looked at the Baoshan and Dehong regions in Yunnan. They were giving technological assistance to coffee farmers to help them grow coffee. They brought in experts to help with the cultivating, technical aspects, knowledge on varieties of coffee beans, and techniques. Most of the farmers had never grown coffee before and it was a new project in Yunnan.

The company's campaign was "coffee in the clouds" which if you visit you would see the coffee trees grow higher on the mountains and they can literally be in the clouds when the weather permits. Yunnan is also the northern most region that grows coffee in the world in the coffee belt that was mentioned earlier. In the end Pu'er was selected. Baoshan and Dehong also grow coffee but Pu'er become the main area for coffee growing in Yunnan. Now there are two coffee processing centers in China with one in Dongguan and the other in Qingdao. Nestlé also used the campaign of "Coffee- A Good Beginning of a Day" when their instant coffee appeared in the market.

In 1991, Nestlé started buying coffee through middle men. It bought about 1,350 bags, each weighing 60 kilos. It also set up an office in Kunming so that it could be in Yunnan and able to reach the farmers easier. In 1994, Nestlé wanted to increase the purchase volume and hired agronomists to help farmers set up and take care of farms. Nestlé trained over 16,000 farmers how to grow coffee and on good practices. In 2002, Nestlé closed its office in Kunming and went directly to Pu'er where most of the coffee farmers are nearby. That way Nestlé could more easily be in contact with its farmers and closer to the coffee. It is important to note here that in 2001 coffee prices were at a historical low at 42.50 cents USD per pound. This was a bad time for the coffee industry and there was little confidence around the world. Nestlé decided to put confidence in Chinese coffee farming when they started buying directly from farmers and a year later they moved their offices to Pu'er.

The Nestlé offices were in downtown Pu'er city and were two apartments converted into offices. It was old, cramped and not suitable for Nestlé. It didn't even have its own

warehouse and shared a warehouse with the local National Grain Warehouse. The equipment it had was also older and manual. In November 2014, the budget was approved for Nestlé to build a coffee center. In February 2015, was the ground breaking and March 23rd, 2016 was the opening of the coffee center. It is equipped with a warehouse, better and newer equipment, a laboratory, offices, training room, many other nice features. The training room is important so they can train farmers on many things including quality and harvest techniques. They also increased the staff from under ten to a total of over 20 people. There are seven agronomists, several in human resources, a receptionist, security guards, and three or four testers.

Coffee farms are as close as ten kilometers or 6.21 miles outside of Pu'er city. It's important to note that Nestlé was not promoting the change from growing tea, or other crops for that matter, to growing coffee. Tea and coffee can grow in the same area but generally they are grown at different altitudes. Coffee is grown at a higher altitude than tea so they don't compete against each other.

In 2016, Nestlé bought coffee beans from 1,434 suppliers. Of those 1,434 suppliers, 89 percent of them were farms composed of less than five acres which accounts for 27 percent of total coffee bought by Nestlé. The other 11 percent of the suppliers were middle men or businessmen that represent a collective group of farmers. This accounts for 73 percent of the total coffee bought by Nestlé. Also in 2016 China was included in the statistics of the USDA on coffee production and China was ranked 11th in the world. Out of the total production of coffee produced in Yunnan, Nestlé buys around 11 percent per year. The other 89 percent is bought by Starbucks, Ecom, Volcafe, a Café group, Louis Dreyfus and Dehong Hogood. Nestlé bought about 12,050 metric tons. Starbucks and Ecom bought about 7,000 MT each while Volcafe bought around 5,000 MT and Dehong Hogood bought about 6,700 MT. The Yunnan provincial government is promoting specialty coffee and even held a specialty coffee competition in Pu'er in March 2017. The Pu'er Coffee Bureau oversees promoting such events. Specialty coffee may bring in more money but less of it is sold and therefore is not suitable for farmers to grow only specialty coffee. They must go with the market demands.

Until now, Nestlé has only made three of its products using solely Yunnan coffee. The three products so far are Nespresso Yunnan Edition in 2004 sold in Europe, Nescafe Yunnan Gift Box in 2012 sold in China, and Dolce Gusto Yunnan Special Edition in 2015 and 2016 sold where Dolce Gusto was sold. Nestlé built the Nestlé Coffee Center to be more efficient and to increase the supply to Nestlé processing centers in China. Most of

the coffee is being used to supply Europe.

Nestlé has a good reputation in the coffee community in China according to the lead agronomist in Pu'er. Nestlé worldwide in 2017 is ranked 54 out of 100 on the Global RepTrack 100 by the Reputation Institute and 36 by Fortune on the World's Most Admired Companies. Nescafe worldwide in 2016 is ranked 36 by Interbrand for Best Global Brands and 32 by Forbes on the World's Most Valuable Brands. The Reputation Institute's 2016 China RepTrak100 did a survey of which company's Chinese consumers like best using seven key factors from products and innovation to leadership and performance as well as data from throughout the year and historical data. Nestlé China received a score of 72.6 out of 100 and ranked 11th. The Chinese consumers like many of Nestlé's products such as chocolate and other sweets as well as coffee. Most of the other top 15 companies in this ranking were in the automotive industry, technology industry or luxury brands and designers such as Rolex, Armani, and Gucci.

Nestlé was the first multinational corporation to enter the coffee market in China. Nestlé and many of these coffee farmers "grew up" together. They have been partners from the start and expanding the market for coffee. This partnership has been good for both Nestlé and the farmers. Nestlé has made a good business out of selling coffee and has started using Yunnan coffee in some of its products. The farmers have also benefited from this partnership because they have gone from making maybe one thousand USD a year to some of them now making over 18,000 USD a year. An agronomist that has worked for Nestlé for almost 20 years said he remembers when he was first going to these towns and villages and how poor they were. The people lived in what the western world would probably call shacks and now many of them have built new houses that are very nice villas and are buying BMW's. I had the chance to visit some of these places and see for myself. Most of the old houses had been taken down but there was one or two still up. One now houses the animals that the farm keeps.

Nestlé tries to be honest and transparent with the farmers regarding what coffee they want or are looking for and how the whole process works. They regularly do trainings for the farmers on the processing of the coffee so they can improve the quality and so that it is up to Nestlé standards and therefore can be sold to them. Nestlé only buys coffee that is 4C approved. The 4Cs are Common Code Coffee Community. These 4C's were developed in 2005/2006 and started to be implemented in 2007/2008. It was hard at first because people don't like change but it creates 100 percent responsible sourcing. These 4C's have to be followed every year and every harvest. It sets basic conditions for

sustainable development of coffee. In 2009, Nestlé realized they were training farmers but they were isolated and in 2010 it put efforts to come up for a global strategy called the Nescafe Plan. In 2013, Nestlé started a scholarship program for the children of the farmers they work with so that they could go to better universities.

Nestlé has also been doing many more recent activities. They have a partnership with Tropical Crop University in Pu'er where they give students one month long internships. The interns learn about the different aspects of the coffee industry and what Nestlé does and how it runs. They are also focusing on the 4C's and increasing the number of farmers that are 4C certified as well as farmers being more efficient. Nestlé is also trying to promote a new way of processing the beans that uses less water to be greener and save water. Nestlé has also become the standard in safety. When the coffee center opened, the company did many safety trainings not only for themselves and the people working there but also for farmers. The Pu'er government has recognized that and has even asked Nestlé to provide safety trainings for some of their staff as well.

Nestlé has plans for the future as well. The Agricultural Services Manager would like to implement more in the coming years. One of the biggest ideas is to promote a new generation of coffee farmers by starting a Nescafe School to teach people about general coffee knowledge, accounting, the market and sustainability spending one week on each topic.

4.3 Business Strategy

Nestlé is run from the corporate office in Switzerland and determines the strategy that will be used to manage the company to be successful. The corporate office works with the three zones of Europe, the Americas, and Asia, Oceania, Africa and the Middle East to ensure that the Nestlé vision is spread worldwide. Nestlé's goal is to be recognized as a world leader in "Nutrition, Health, and Wellness," and be viewed and trusted by all the stakeholders involved. Nestlé's business strategy has been created around their core principals of Good Food, Good Life, and Creating Shared Values. They want to make money since they are a business but they also believe in giving back. Nestlé's business strategy also includes the Nestlé Strategic Roadmap, marketing and corporate social responsibility. Part of Nestlé's strategy is to play the long game where they strive for opportunities and success but believe that it must sustain the shared values to be successful in the long term.

Nestlé focuses on "Nutrition, Health and Wellness" as stated in many of their

company documents and on their website. They believe that since nutrition is so important to the everyday life of people, they want to help benefit their consumers through the products and services they offer. Nestlé has over 150 years' experience and tries to adapt to the ever-changing markets by taking advantage of the opportunities given to them to achieve success. As part of the focus on nutrition, Nestlé has programs such as United for Healthier Kids that helps teach healthier eating and drinking habits as well as lifestyle habits. The Nestlé Healthy Kids Programme teaches about nutrition and about the importance of staying active. Nestlé itself is trying to reduce sugar, saturated fat, and salt to keep its products healthy.

Nestlé believes that as part of their business strategy that they need to keep themselves “relevant in this fast-changing world, we can deliver industry-leading growth. We work with agility, creativity and discipline, constantly innovating and renovating our portfolio (Nestlé Strategy).” Nestlé uses their research and development across all their products to try to maintain a leading position in the market. Nestlé holds a 22.4 percent of the market share in the global coffee market (Postma, E., et al).

The Nescafe strategy includes winning products to deliver coffee enjoyed by Chinese consumers, availability so that Nescafe is where the consumers are, and communication by engaging the consumers. Nestlé has a wide variety of coffee products in China. They have in and out of home instant coffee for the mainstream consumer, they have ready to drink Smoovlatte as well as Nescafe Premium instant coffee for the mainstream consumer plus other consumers, and they have several brewed coffee machines for premium products such as Nescafe Milano, Nescafe Gusto, etc. The range of products means that consumers can drink Nescafe whenever, wherever and however they want. Consumers can make a variety of different coffees at home, at work, at the office, or pick up a coffee at a Lawson's or 7-11 at any time. The communication strategy is to engage the consumer specifically the younger generations and encourage them to experience coffee. The company also works with brand spokesperson Han Han who is China's most popular blogger and has seven million fans (Schipper, H. 2012).

4.3.1 Nestlé Strategic Roadmap

Nestlé Strategic Roadmap is what Nestlé uses to help guide the company. It demonstrates the company's idea of what the company should be and wants to be. The company believes in “securing progress today and ensuring success in the future by achieving simplicity, investment for growth, scale benefits, and driving performance (Kalbus, E., 2011).” The roadmap portrays “what we want to leverage as competitive

advantages to fuel growth, where we want to grow and how we will do that efficiently, effectively, and responsibly. It drives internal alignment behind our goals (Nestlé Strategy).” This means that this roadmap is used for employees to help Nestlé reach its goals through competitive advantages, growth drivers and operational pillars.

The competitive advantages are people, culture, values and attitude, unmatched geographic presence, unmatched research and development capability, and unmatched product and brand portfolio. The growth drivers are Nutrition, Health, and Wellness, emerging markets and popularly positioned products, out of home consumption, and premiumization. The operational pillars are consumer engagement, operational efficiency, innovation and renovation, and whenever, wherever, however.

4.3.2 Principles of Business Operations

Nestlé has ten corporate business principles as listed on the Nestlé website. Nestlé created these principles throughout 140 years of operations and weren’t formally published until 1998 when the company published a document, but were unofficially established and in place for quite some time before then. They have since then added and updated the principles such as adding the United Nations Global Compact principles and revising them to add more details and guidelines. These principles are integrated throughout the entire company.

The first principle is “Nutrition, Health and Wellness.” This is the core aim of the company and they work to create more nutritional products that not only taste better but give consumers more enjoyment.

The second is quality assurance and product safety. Nestlé tries to deliver safe products and high standards to consumers around the world. They take their commitment very seriously to always produce safe products. Their quality policy says that “to build trust by offering products and services that match consumer expectation and preference; to comply with all internal and external food safety, regulatory and quality requirements.”

The third is consumer communication. Nestlé is committed to responsible, reliable consumer communication because their core business strategy is centered on helping people have better, more balanced and healthier lifestyles and diets. In the Nestlé Consumer Communication Principle, it specifies that all marketing communications must accurately represent and portray foods that does not promote over- eating. It also doesn’t allow for marketing to children under the age of six years old and the marketing of products to children between the ages of six and twelve is restricted to products that “meet predetermined nutritional profiling criteria, including limits on energy and

health-sensitive ingredients such as sugars, salt, saturated fat, and trans fatty acids.” The company tries not to market to children so as not to mislead them or give unrealistic expectations. For the marketing of infant foods, the company recommends breast feeding but provides alternatives that meet international standards for those who cannot. This marketing complies with the WHO International Code of Marketing of Breast-milk Substitutes.

The fourth is human rights in their business activities. Nestlé follows and implements the United Nations Global Compact’s regarding human rights and labor to be an example of good human rights and labor practices. They also uphold the eight fundamental Conventions of International Labour Organization that protect workers along with several other policies from organizations around the world to guarantee human rights.

The fifth is leadership and personal responsibility. This principle applies to employees of Nestlé in which treating everyone with respect and dignity is expected. Nestlé also hires and promotes people who uphold these values and does not accept any kind of harassment or discrimination. The full details can be found in the Nestlé Management and Leadership Principles that describe the culture and basic values that all employees need to uphold.

The sixth is safety and health at work. Nestlé is very proactive on safety with an example in Yunnan as expressed earlier. There are more details in the Policy on Safety and Health at Work that lays out safety as a priority.

The seventh is supplier and customer relations. The Nestlé Supplier Code goes into detail about the standards they require and talks about business integrity, sustainable operating and agricultural practices, labor standards, safety, health and environmental practices. They also include the right to verify the compliance with this code.

The eighth is agriculture and development. There were examples of this is China with the dairy and coffee farmers. Nestlé wants to improve agricultural production, rural communities, economic status of farmers and make them more environmentally sustainable. They also apply their quality and safety standards to this area as well.

The ninth is environmental sustainability. Nestlé tries to be environmentally sustainable and have sustainable business practices. They aim for efficient use of natural resources, sustainable use of renewable resources, and zero waste. The entire principle is outlined in the Nestlé Policy on Environmental Sustainability and uses policies from the United Nations Global Compact.

Lastly, the tenth is water. Nestlé tries to use water sustainably and improve the management of water. Their commitment in the Nestlé Commitment on Water policy details their priorities and objective regarding responsible water consumption.

4.3.3 Marketing Strategy

Nestlé, as part of their marketing strategy, tries to diversify so that they are not limited to just one product. Coffee is an important product for Nestlé as they have many coffee products.

The Boston Consulting Group or BCG came up with a matrix to show market penetration. This is useful to understand the potential of different business units being managed by an organization. This approach determines whether a product is a question mark, a dog, a star or a cash cow and is useful to see where coffee falls on the chart.

First a question mark is a product that has high market growth but low market share. This means that a company must decide whether to increase the investment into the product and what to do with the opportunities it has. This product will grow rapidly in the market but also consume a large amount of cash. It won't generate a lot of cash but has the potential to be a star. A dog is a product that has low market share and low market growth. This means that it is weak in the market and it is difficult to make a profit on these products. This product neither generates nor consumes a lot of cash. Next, a star has high market growth and high market share. This means that this product is doing very well and also has many opportunities. This product both generates and consumes a lot of cash but if it can maintain its market share then it will become a cash cow. Lastly, a cash cow is a product that has low market growth and high market share. This means that this product is in the mature stage of its market and has a high rate of return. This product provides the cash flow to turn question marks in market leaders.

Nestlé Nescafe worldwide is considered a cash cow due to its market maturity. It has had strong performance and continues to maintain its market share. This market continues to be lucrative for the company. Nescafe in China would be a star. Nestlé Nescafe has a high market share and has a high market growth. Every year the consumption of coffee is growing in the double digits and the instant coffee market makes up over 99 percent of the coffee market in China with Nestlé Nescafe having 68 percent of the instant coffee market in 2009 and 66 percent as of 2016. It continues to maintain its market share. This is good for Nestlé since Nescafe in China can be a cash cow in the future. In other more mature coffee markets, Nescafe is already a cash cow. Nestlé is investing a lot into the coffee market in China but it is also receiving a lot of money in profits.

There are three growth strategies that Nestlé uses. The first is a transnational strategy that has low cost, different products, different markets and high local responsiveness. The second is a localization strategy that uses brand name recognition resonates locally in different cultural. The third, is customization by producing and selling goods that have been adjusted to satisfy consumers of different needs in different markets.

Market segmentation includes geographic, demographic, psychological, and behavioral. Geographically, Nescafe can be drank year-round around the world. Nestlé did come up with using iced coffee for summer and classic warm coffee for winter. This hasn't reached China yet, due to the lack of coffee culture. Demographically, Nescafe is drank by the younger generations from college to middle class working adults. Additionally, Nescafe is drank more by people exposed to Western culture and lifestyles. Nestlé also has tried to provide a product for everyone. They have the Nescafe instant packets for the everyday worker and the Dulce Gusto for the middle class and are more coffee cultured while also enjoying brewed coffee. They also have a high-end Nespresso for the wealthier individuals who enjoy a cup of brewed coffee. In the psychographic segmentation, Nescafe instant coffee caters to the busy lifestyle of people not only in China but worldwide. They have the higher end coffee for those that just want to enjoy a cup of coffee. Behaviorally, Nescafe is for waking up in the morning, staying alert and focused at work or studying and an afternoon pick me up. It also has some health benefits such as increased metabolism and energy.

Positioning strategy Nestlé has a lot of products and uses product differentiation to target different customers. They also use channel differentiation by using expert mark salesmen and transportation to get their products to the customers. Image differentiation with Nestlé having a logo that is different from others and is very recognizable. People differentiation with Nestlé focusing on people by training and educating them. Service differentiation with Nestlé having a 24-hour hot line service and better service than competitors.

Marketing mix is one of the most common tools for a company to realize its marketing purpose in the target market. The marketing mix is the 4Ps which are product, price, place, promotion. The elements of 4Ps are a successful marketing strategy that provides more information about the features of products, affordability of price, the promotion budget, and distribution channels. Nestlé has many products but this paper focuses on coffee, such as instant coffee, brewed coffee, coffee-mate powdered milk. Place is where the products are sold and Nestlé mainly sells their products in all the

leading stores in big and small cities. They have a good distribution but are dependent on farmers and need a space to roast and process. In expanding the market, companies must use their distribution channels to get products to the market quicker. They also have online shops to buy Nescafe. Price can be defined as the value a product attributes in terms of money the consumer is willing to pay or expects to pay in exchange for the product. Nestlé tries to make affordable products that are also good quality as well as some higher quality ones so that they can target more people. The company really taps into the market with the most variety of products being instant coffee. Coffee is a commodity so it is dependent on the consumers and can be very volatile. Promotion involves the product and how it is promoted. Nestlé has the Nescafe plan to promote its coffee. Nescafe may have samples in the store or there may be a contest such as win an iPad or buy this package and get a Nescafe cup. Nestlé has a blogger to help with their marketing in China and they do many programs in the communities they are in. This raises public awareness in those areas and across China (Wei, 2016).

4.3.4 CSV

In 2015, Nestlé celebrated 150 years and looked back on the foundation of the company by Henri Nestlé who founded the company to save the lives of infants. The company has lasted for that long because of their respect for people, cultures, environment, and the future. This leads us to one of Nestlé's fundamental values, which is Creating Social Values or CSV and means that they believe that for the company to be successful for a long time, then the company needs to create value for itself, its shareholders, and society. Nestlé has many programs that help the people around the world through nutrition, health and wellness.

CSV shapes the business strategy of Nestlé as demonstrated in this section Nestlé is very concerned about the environment and well-being of people worldwide. Nestlé has a Creating Shared Value Council that consists of 13 members that have expertise in CSR, strategy, sustainability, nutrition, water and rural development. The Council advises Nestlé on the best ways to implement CSV and assess the progress of the company. Nestlé also has Stakeholder convening's and events where they look to understand, develop, and improve their policies and commitments. These convening's are organized and hosted by external experts and ensures independent opinions and feedback. Nestlé even has a Creating Shared Value Prize that is awarded by the council every two years. The award has eight criteria and is open to social and private enterprises as well as NGO's. The eight criteria are innovation, environmental sustainability, impact and results,

replicability, scaling up, organizational capacity, potential for CSV and impact of the CSV prize funding. Every year they publish a CSV performance titled, Nestlé in Society: Creating Shared Value. The document is very detailed with 351 pages and lists everything from business principles and partnerships, human rights and rural development to water and environmental sustainability.

Harvard Business Professors Michael Porter and Mark Kramer wrote "Creating Shared Value" for the Harvard Business Review in 2011. Together they created the idea of creating shared value that involves creating an economic value for both the company and society by helping or addressing needs or challenges. According to them, companies are too focused on social responsibility where companies help society by donating money but not by helping at the core or the root of the problems. The company's focus on their own images rather than helping social progress and they should be looking at it as a driver of productivity instead of as a look good, feel good response to pressure. Porter and Kramer wrote that Nestlé was one of the top-ranking companies for creating a real shared value for the company and society in many aspects of their business. Porter and Kramer assert that Nestlé has an approach that has already shown to be long lived and will continue to live because they are creating a value for everyone. In 2015, they showed that this strategy helps to drive growth and success while also addressing societal issues like water, rural development and sustainability. It was taught in a class in December of 2015 and is going to be taught in Business Schools around the world.

There are two examples of this is Nestlé's history in China. They first helped dairy farmers in the north of China with training in taking care of cows and better practices. The second example was in Yunnan with the coffee farmers where they again trained and help the farmers learn about coffee growing and procedures. They then also bought from the farmers they were helping by giving them direct access to raw agricultural materials. This helped both Nestlé and the farmers as well as the region in general. To this day, Nestlé has a good relationship and good standing in those areas.

Nestlé focuses on water due to the fact that lack of water will be a real issue in the future especially if no one is doing anything to try to conserve water or cares about what happens in the future. Water is the most important resource on the planet, as human are made up of over 50 percent water and need it to survive. Therefore, they try to not only raise awareness on water conservation because access to clean drinking water is vital but also improve access to water and sanitation in their value chain. The company also focuses on rural development because helping farmers and communities also helps the company and helps them educate others on sustainability. The company tries to

implement responsible sourcing of their supply chain and to continuously improve their green coffee supply chain. Environmental sustainability is also important to the company and it tries to improve resource efficiency, the environmental performance of packaging, the environmental impact of the products and provide accurate environmental information. The company heavily emphasizes nutrition, health and wellness as mentioned earlier, it is the very core of the company. Nestlé substantially invests in research in nutrition and health, is reducing unhealthy ingredients, promoting physical activity and hydration, and providing education programs.

Nestlé also has tried to protect the environment around its many factories and invests 100 million CHF on average per year on protecting the environment. Nestlé tries to limit its effect on the environment by using a minimum of resources while at the same time producing the maximum amount of goods and trying to reduce its waste and emissions. Nestlé also has over 800 agronomists, technical advisors, and field technicians that provide assistance to farmers around the world to produce better quality products as well as efficiency and impact on the environment. In Yunnan now they are trying to reduce the water consumption to save water and be more efficient in the future.

4.3.5 CSR

Nestlé has been doing Corporate Social Responsibility since the company started. Since its core value is CSV this basically replaces CSR. As stated in the previous section, Porter and Kramer have said that CSV goes beyond CSR. CSR is not enough for companies to do anymore. In this day and age, people want companies to be more engaged and active in society and responsible for their impact on not only society but the environment.

Before 2005, Nestlé didn't publish or promote its efforts in Yunnan. After 2005, the company started promoting its CSR to show what it was doing in the region. Nestlé used the ideas of developing a value chain and doing corporate social responsibility together to not only help them make money but to get a good reputation. Nestlé helps the locals earn more money and get them out of poverty, can buy local and therefore lower costs and call it goodwill investment that gives the Nestlé brand a better image. Nestlé's "creating shared values" is a major point of the company's CSR efforts. Under this creating shared values they try to address five global issues: nutrition, rural development, water, environmental stability and people, human rights and compliance. Nestlé believes that for a company, especially Nestlé, "to be successful long term and create value for its shareholders that it must create a value for society (Nestlé publications)."

5 Methodology

5.1 Theoretical Basis

5.1.1 PEST

A PEST Analysis is one of the most common analytical tools to assess markets, specifically the Chinese market environment. This is an analysis of macro-environmental factors that help companies with strategic management. They include Political, Economic, Social, and Technological factors. These factors have an impact on the performance of a company as well as internal resources and industry factors. These factors are useful when company's want to enter a new country or start a new venture so that the company will know how these factors will affect the performance and business activity in the long-term.

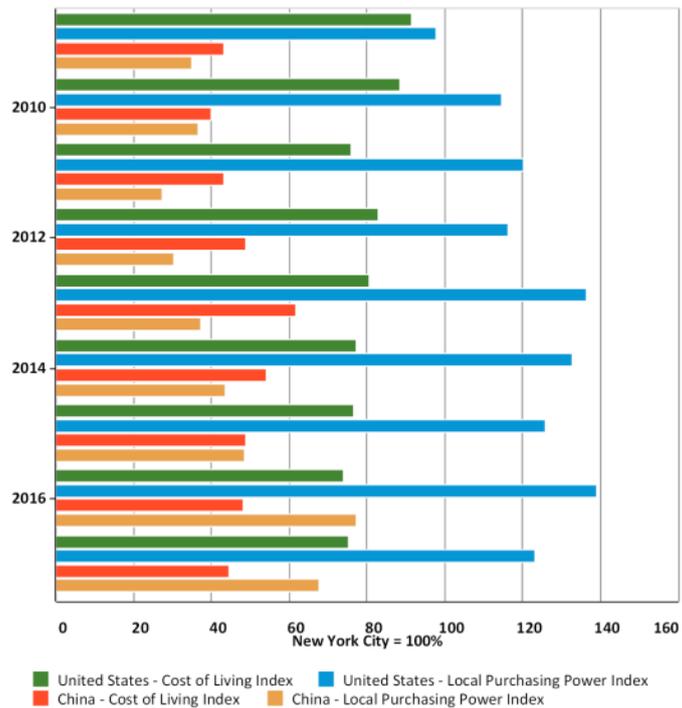
① *Political Factors*

The political factors in China include how the politics as well as government regulations in the country affect business. It also includes how much government intervention there is and any legal factors. In this case, China has been open for foreign investment since 1992 and many laws and regulations have been adapting to more and more businesses coming to China and entering the market. There is more ease and convenience with the improvements. For example, in September 2014 the State Council declared that it would promote and strengthen its policies on imports. This policy affects the importing of technology, products and services and would ease the importing of coffee beans. Furthermore, in July 2015 Shanghai piloted a Free Trade Zone and established a Shanghai Free Trade Zone Coffee Trading Center. This Trading Center could help the Chinese coffee market by not only helping China enter the world coffee market but later on become world player as well. China is also a member of the WTO or World Trade Organization which has helped China promote the importation and exportation of coffee beans. China has a good legal environment for companies as well as some laws protecting companies from unfair competition, and customer's legal rights. Nestlé entered China over 20 years ago and enjoyed preferential policies and treatment such as lower tax rates. This has helped Nestlé to grow and expand at the rate they did (PEST Analysis of China, 2016).

② *Economic Factors*

The economic factors include China's GDP or Gross Domestic Product and Foreign Trade. It also includes inflation, interest rates, economic growth and unemployment rates. China has the world's second largest economy by nominal GDP at 11.3 trillion USD behind the US at 18.56 trillion USD and the biggest economy in the world in terms of purchasing power parity or PPP at 21.27 trillion USD surpassing the US at 18.56 trillion USD according to the IMF.

Cost of Living Index by Country, 2017



China's economy is still rapidly growing as well (Graph: Cost of Living Index by Country, 2017, Appendix A10). There is much room for growth in development as well as trade and investments. The services sector of the economy is increasing every year and the average yearly salary is also increasing every year. In 1985, according to the World Bank the average income per capita of urban residents was 739 yuan. The salary has more than quadrupled since 2002 when the year salary was just over 7,700 yuan which at the 2017 conversion rate is only around 1,118 USD a year and the 2002 conversion rate of approximately 8.2 that's roughly 939 USD a year which is extremely low (tradingeconomies.com). There is a lower cost of living in China compared to Western countries such as the US.

As of 2015 the GDP per capita reached an all-time high with nominal GDP at 8,140.98 USD a year and the GDP based on PPP per capita at 14,339 USD according to the IMF. This increase in GDP resulted in a many people at poverty level moving to the middle class and changed the distribution of classes in China. The largest segment became the lower middle class. The average yearly gross salary in China reached 10,000 USD a year and the average net salary reached 8,000 USD a year while the average gross and net salary of the US was 49,000 USD a year. The East coast grew much faster than the middle and western parts of China due to access to ports, and cities like Beijing and Shanghai being on the Eastern Coast. This new growth and shift to the middle class gave

people more purchasing power and shifted China from a rural populated country to a city and suburb populated country. This has increased demand for products starting out with running water, bicycles and wrist watches to thousands of luxury goods like cell phones, name brand products and services across all sectors (Graph: Barton, D., 2013, Appendix A11).

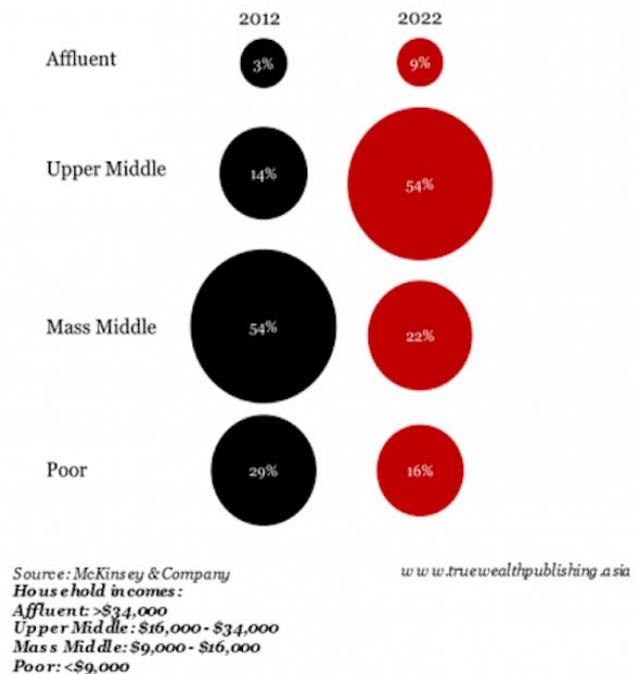
As of 2010, China had been the largest exporter of goods. China changed from a closed economy to a market economy in the 1980s when it opened up its economy to the world. As a result, China has also been the recipient of foreign direct investment (FDI) since then and increased rapidly from 2004 to 2008 and then again from 2009 to 2011. There was a drop from 2008 to 2009 but it has since recovered (World Bank). The Trading Center mentioned in political factors also helps the Chinese economy especially in Shanghai because it brings it to the global market and leads to more development.

Nestlé benefited from this factor as well. Nestlé entered in the very beginning of the Chinese development and therefore received the benefits of low costs, improvement of the investment environment, rapid economic development, and the increase in income and purchasing power. Nestlé is shifting its focus from its mature markets in America and Europe to Asia and the Middle East. This is a smart business move considering the room for growth and the predicted number of the middle class by 2020 in China (PEST Analysis of China, 2016).

③ *Social Factors*

The social factors include education and tourism as well as demographics and lifestyles. Since China's economy has been growing and more and more people are entering higher social statuses, the number of students at universities has also increased accordingly. From the studies that have been done on consumption in China, the majority

China's Middle Class as Percent of Urban Households



of the coffee drinkers have a higher education. In the main cities like Beijing and Shanghai, the Chinese have been exposed to Western culture for quite a long time and therefore have become accustomed to the culture including coffee. Coffee culture has been spreading to the other cities in China due to the foreigners that are living there, the spread of Starbucks and Western culture and the instant coffee products of Nestle. China's tourism industry is important in the case of the spread of coffee. This is because since China has opened its economy and its grown to be the second largest economy in the world along with the ease of travel and lower cost, the number of foreigners who visit China has increased drastically. In 1978, there was only about 200,000 foreign visitors and in 2014 there was over 128 million visitors. With this many visitors, there has been an increase in Western products and culture and many hotels have also grown accustomed to serving coffee (EU SME Centre, 2015). Nestlé also tries to cater to the local market and the consumer tastes. In China, the company looked at the Chinese culture and tried to make products for the consumer such as the variety of instant coffee products.

④ *Technological Factors*

The technological factors are how technology positively or negatively impacts business including technological advances and the role of the internet. China's technology industry is very advanced. China went from paying with cash only to paying with debit cards and now the use of mobile pay through various platforms. These different platforms are so widely spread you can buy food on the street using Alipay or WeChat Pay which are the two most common application for electronic pay. WeChat is also the biggest social platform in China and users can do everything from messages, using China's version of Facebook, and sending money to paying bills, movies tickets, ordering food, etc. Starbucks this year even added a gifting of coffee option to the platform. The Chinese have become very accustomed to technology and e-commerce is one of the most popular way to buy products online as well as it is one of the best ways to advertise. November 11th also known as 11.11 or Single's Day is one of the biggest online shopping days of the year very similar to Cyber Monday in America. Single's day in China in 2016 hit a record high for its sales on that day. It reached almost 12 billion USD by 12pm. It took less than seven minutes for Tmall (an online site of Alibaba) to reach ten billion RMB in sales compared to 2015 when it took 12 minutes and 28 seconds to reach the same amount. When Single's Day started in 2009 Alibaba's sales only reached 8.17 million USD. Technology plays a big factor in the market and can be used to a company's advantage. It should be mentioned that the Chinese government does monitor and determine what sites

are allowed in China. As long as a company gets government approval then this is not an issue.

Nestlé has the largest research and development network of any food company worldwide. The company is continuously looking to create new products, improvements on current products, and new marketing strategies.

In conclusion, China is a good market to enter with little risk. The rapid economic growth and stable political condition make it a lucrative market especially in the e-commerce industry. If China's economy can continue its growth and with the rising number of people in the middle class, the Chinese market is a good investment for the future. Some challenges include differentiation in a country where there are several brands of every product, legal protection, and cost reduction in the tides of rising incomes and purchasing power.

5.1.2 SWOT Analysis

The previous section looked at outside factors in a PEST analysis, while this section is an internal environment analysis of Nestlé as a company. This analysis is a SWOT analysis, which stands for Strengths, Weakness, Opportunities, and Threats. This is to help give the reader and the author a better understanding of Nestlé as a company. Nestlé has many products and companies so this is a general analysis for the company as a whole, but also looking at a SWOT analysis of the Nestlé in China.

①Strengths

The first category is strengths. One advantage Nestlé has is that it has a broad brand and product portfolio. Nestlé has acquired numerous companies and products since it started in 1866. This means that if one product or company does not do well or performs poorly, then the company as a whole will be fine because it has many other products and companies within it to make up for one or two poorly performing products or companies. As mentioned earlier Nestlé's products span from various foods to pet care and weight management. This span of products across the board make Nestlé versatile and means that Nestlé has at least one product for everyone. Nestlé is not limited to one specific area of products or one specific region.

Nestlé also has a significant number of research and development centers around the world. Nestlé even established the Nestlé Food Safety Institute in Beijing in 2014 as previously mentioned. The company has also heavily invested in its research centers in the US, Singapore, China, and many other countries. In 2013 alone, the company invested 1.5 billion CHF on research and development activities. With the numerous companies

and products, the company must also be looking to the future and to provide new and innovative products to continue to keep revenue sources. Another strength for Nestlé is that Nestlé is also worldwide. The company has 447 manufacturing plants in 86 countries and conducts business in 196 countries. This distribution spreads the risks of doing business. If one market does poorly, they have the others to fall back on. Some markets are more important than others because of the market share that Nestlé has in each with the US being the largest market for Nestlé with a little over 25 percent of their business in the US and China being the second largest market for the company at 7.2 percent. So, as you can see there is a significant different in the amount of business that the company does in various markets, but they can help balance each other out when one does poorly. It is a strength to do business worldwide because the company can then reach a wider geographic area and expand.

Lastly, Nestlé has a debt to equity ratio of .35 as of 2013 which means that they decreased this ratio from .45 in 2012. The most likely reason for this is that in 2012 the company's equity was over 61 billion CHF and increased 2.57 percent in 2013 to 62.5 billion CHF. This is good for the company because they have less debt and are decreasing it yearly. It also means that the company has enough equity to pay its short-term debts if they were demanded. This is important for businesses so that the company is never at a disadvantage or unable to pay its debt.

② *Weakness*

One area of weakness for Nestlé is since it has a broad number of products and companies, it also has product recalls. This can be very costly, especially in the US when people decide to sue the company. It costs the company money to recall the products of course, because the company must pay for the recalled products to be returned to the company, but also on top of that, there is a cost to the reputation of the company. If a serious recall happens then consumers might lose confidence in Nestlé. Nestlé has had a few recalls that can be considered serious. The first is in the US where the company recalled Lean Cuisine's Mushroom Mezzaluna Ravioli in its Culinary Collection because of the potential of glass fragments in the product. Another recall in the US, was the recall of Nesquik chocolate powder because the products that are used to make the brand had the presence of Salmonella. Third, in Italy and Spain, the company recalled two chilled beef pasta products after tests found there were traces of horse meat in the products.

The second weakness is that the company has a declining operation performance. In 2012, the operating margin was 14.92 percent and in 2013 was 14.18 percent.

Furthermore, the company had a decrease in net margin from 11.4 percent in 2012 to 10.87 percent in 2013. This decrease can only be attributed to improper cost management or the company not focusing as much on being profitable and possibly more on other things. Another concern, is the complex supply chain and maintaining that relationship with the farmers. The company has many local supply chains that they depend on to make their products. This could have a negative impact on the company and its operations if there were to be a problem with supply chain or the relationships.

③ *Opportunity*

In over 100 years, Nestlé has acquired, partnered, and sold various companies and products. This led to Nestlé becoming the diverse company that it is. The company has been investing in new factories, research centers, and programs on maintaining health. Nestlé has also been acquiring services such as Petfinder, an online database that links adopters with pets and Pamlab that offers medical food products under medical supervision in the nutritional management of patients. These acquisitions are strategic for the company and help strengthen parts of its business. The company can increase profits and technology as well as expanding geographically and enhancing its core expertise's.

The second opportunity is increasing global food consumption. Many countries around the world are increasing their per capita food consumption due to raises in income and development within the countries. From 1997-1999 the kcal per capita per day was 2,681 in developing countries and increased to roughly 2,805 in 2015. This is an advantage for two reasons. The first, is that with increasing income comes increasing purchasing in general and Nestlé sells many products including food products. Second, if people are consuming more than there will be more demand for products. Nestlé is also very involved in the development of many different areas of the food industry.

The last opportunity is new products. Nestlé launches many products throughout the year including but not limited to different coffee products such as a large cup system for the US and Canada and candy for special events like the Super Bowl and holidays such as Easter and Halloween. These new product launches give the company extra revenue and expand its consumer base because in the US it would be hard to find someone who doesn't buy candy for Halloween or Easter as they are the biggest candy holidays throughout the year.

④ *Threats*

There are many threats to companies especially with such a global interconnected world. The first threat is expansion by competitors. There is a great deal of competition in

general both locally and from other multinational corporations. If other companies expand, it could put pressure on Nestlé as well as their market position. An example, is Nestlé's competitor Danone when they increased their stake and interests in Chinese dairy. Danone signed an agreement to start a joint venture to produce fresh dairy products and another joint venture in chilled yogurt products in China. Nestlé has been in the dairy business in China for quite some time. Danone has been expanding and gaining significant advantages from its two joint ventures. This forces Nestlé to look at itself in China, its pricing, its strategies, and its position in the market. There is also the volatility of commodity prices since Nestlé is mainly in food processing.

The second threat is stringent regulations. This means that there are specific laws and regulations pertaining to specific products in specific countries. For example, in the US the food, drug and cosmetic industry are regulated by the Federal Food, Drug, and Cosmetic Act or FDA. The FDA conducts investigations and examines products to make sure they comply with the regulations set forth in the act. It was set up to safeguard all products and people. It can be very costly to comply with these regulations but if companies don't comply, then there are significant fees and penalties as well as damage to the company's image.

The last threat is foreign exchange risks. This is very important because Nestlé operates in 196 different countries, most of which have a different currency. Each currency changes its exchange rate daily and while although it is usually minor, it can be enough to affect Nestlé. Since Nestlé is a Swiss company, it uses the Switzerland Franc or CHF when reporting its financials. This makes it hard for the company because each country's financial must then be converted into CHF. In 2013, Nestlé had a loss of 173 million due solely to foreign exchange rate differences. Some currencies are stronger than others and that means that some currencies perform better than others. In China, for example, the exchange rate between the yuan and the CHF is almost seven to one. That means that while although the Chinese market might be doing well, once converted into CHF it doesn't appear to be doing as well as other countries. That being said, the company loses money when currencies fall and more of a currency is needed to reach the same amount in CHF. When this happens, the company sees a drop in its profits margin (Canadean Nestlé S.A., 2015).

5.1.3 Porter's Five Forces

Porter's Five Forces model is a tool to analyze the industry and develop a business strategy. There are five different factors which are threat of new entrants, threat of

substitute goods, bargaining power of suppliers, bargaining power of customers and competitive rivalry within the industry. These factors help to determine a market's attractiveness, its productivity, strengths, and weaknesses. This model is widely used and helps to explain why certain industries are profitable.

① *Threat of New Entrants*

New entrants face a unique threat in the market, especially if the market is attractive. Depending on the market there could be restrictions or limitations which would make it difficult for new entrants to become established in the market. Nestlé is a very large company with products in many different markets, and has a strong brand name. There are already many other companies in these markets who have gained market share, specifically the food processing industry. Nestlé however, still has a large market share. While there is a threat to an of new entrants, due to the number of products and brand name of Nestlé, this threat is moderate. Nestlé in China has also been around since the 1980s and with such a long history as well as consumer satisfaction the company has a large market share. Nestlé also has the majority share in instant coffee market, and has become the name for instant coffee in China.

② *Threat of Substitute*

Similarly, the threat of substitute is also always a factor. Every product has a substitute, but it depends on the product. The quality and the competition determines if it is really a threat. Nestlé has many products, so this force is especially important. Nestlé has to work to keep from having threat of substitute or being replaced. Recently, more and more companies are producing or introducing products that have less artificial sugars and processed ingredients such as organic or whole foods products. People are starting to care about what they are putting into their body and that creates a threat of substitutes. This is one reason why Nestlé does so much research and development so they can continuously research, develop, and make better products. The Chinese market no matter what product, deals with of competitors with similar products. There are a few substitutes such as Maxwell, but Nestlé by far overcomes this challenge and has the most choices and options when it comes to instant coffee.

③ *Bargaining Power of Suppliers*

The bargaining power of suppliers is another important factor because suppliers have products or ingredients that company's coffee needs and this is a main strength of the company. Nestlé China's strength is due to its strong relations with suppliers specifically within and in particular China with its coffee and dairy suppliers. Nestlé uses its CSV

model to create lasting partnerships. Nestlé has many options when buying coffee since they have operations worldwide and buy coffee from many different countries. That being said, Nestlé has created a strong partnership with coffee farmers in China, and buys a fair amount of coffee from them.

④ *Bargaining Power of Customers*

Customers have a lot of bargaining power, because they are ones buying the products. Ultimately, if they don't buy a product then it doesn't continue to be made and falls of the market. On the other hand, for that to work the customers need to work collectively to do so. This is one reason company's try keep and improve their good reputation. They use CSR or CSV so that customers will continue to buy their products. Nestlé incorporates CSV and also tries to create healthier products to increase customer usage, keep their current customers happy, and then expand their market. In the coffee market in China, Nestlé has a good reputation and is one of the only choices.

⑤ *Competitive Rivalry*

Every market is competitive to some degree. Some markets are extremely competitive and other markets therefore have little competition while maintaining the status quo. Competition is good for all parties involved because this creates at least two companies will be competing for customers meaning that pricing will be good and there is more than one choice. The food processing industry has several major competitors such as Nestlé, Kraft Foods, and Groupe Danone. This industry is very competitive, and all of these companies spend a great deal of money on marketing and advertising. In China, Nestlé has a few competitors but Nestlé remains the main instant coffee brand.

6 Independent Research

A questionnaire was decided on to see how people felt about Chinese coffee. This is important to this thesis because it tries to prove that companies want to use Chinese coffee in their products and bring it to the world market in the future. Therefore, it is important to see what people inside and outside of China think of Chinese coffee and the quality.

I also decided to reach out to Nestlé China to see if they might be able to answer some questions so that I could gain more insight into the company. This is important to this thesis because I want to have all the information about regarding my thesis that I can get. There hasn't been much research on Nestlé China as a company or their activities in China. As it turned out, I not only received information about Nestlé China's history and what the company does presently, but I also was invited to visit Yunnan and see for myself first-hand what is going on.

6.1 Field Investigation: Yunnan Visit

In the beginning of March of 2017, I went to Nestlé's offices in Pu'er to see for myself what was going on. I was interested to see what coffee cherries and beans look like before it becomes the liquid that so many are addicted to drinking, as well as, getting inside information. There wasn't much information readily available on Nestlé in Yunnan. It was also very exciting to be able to talk to Nestlé's Agricultural Services Manager of Coffee in Pu'er. He provided very valuable information as well as gave me first-hand knowledge about not only Nestlé in Yunnan, but also, the coffee industry as well.

I learned about the whole process from seed to cup. During the drying process, some beans the farmers have will be placed in piles to be sold to Nestlé because they meet the requirements, while others will be in separate piles to be sold to other buyers. After this, the farmers bring the beans to the Nestlé Coffee Center, either all the beans they want to sell to Nestlé or they bring a sample for testing. Nestlé looks for a certain quality of bean and only buy beans that meet the requirements. Then a sample of the beans goes through testing. They check bean size, whether the beans are broken or damaged, discoloration, and moisture content. Then they are roasted and ground and ready to be sampled. The same process goes for taste tasting and aroma, if the taste of the sample is good then it will receive a three, but if it is off, then it will be marked as fermented, moldy, etc. There

is also a reference sample that the company provides to each testing center so that they can judge whether a sample is equal to or similar to the quality Nestlé is looking for. I was also given permission to do my own taste testing to get an idea of how they determine which samples to buy and which ones are not good.

This trip was good for the research of this paper as it provided a great deal of information that could not be found anywhere else. I was given access to everyone in the offices, tour of the warehouse, information about Nestlé in Yunnan, and exclusive tours of different farms that Nestlé works with. It was also good to be able to get first-hand experience to talk about the research topic. I was also able to try Nestlé's Yunnan coffee products while I was there, which allowed me to get a sense of the flavor and quality of the beans.

6.2 Questionnaire

Independent research was decided on to not only add to existing research, but also to get a better understanding of the coffee consumers. The research is divided into two parts. The first part is a qualitative study and this was chosen to collect precise and correct information face to face. It is useful because it is more personal and the interviewer can see facial expressions as well as detect inflections and understand emphasizes in the interviewees speech. These were semi-directive interviews consisting of four foreigners and two Chinese. This was decided based on the fact that foreigners out drink Chinese in terms of coffee at a minimum of over 160 cups per capita to three cups per capita respectively.

A detailed methodology for this sample consists of the objective of determining if people are willing to buy or drink coffee produced in China. A printed guide is listed in the Appendix B1 that was used to ask the questions to our sample group. The interviews were in April of 2017 in Chongqing, China at a café. The length of each interview ranged from 30 minutes to 45 minutes. The aim was to analyze this data and draw conclusions based on this sample to do the second part which consists of the questionnaire. The printed guide was based on the funnel technique so that the questions started out general to get an idea of the interviewees buying and consumption habits as well as their psychological price. The interview ended with more precise and detailed questions.

This study uses a sample of six people. It was also decided that the sample should be three females and three males based on previous research that shows that participants in the survey were almost equally represented by gender. This sample then consists of four

foreigners with two being female and two being male and two Chinese with one being female and one being male. It was also decided that due to previous research and data that the younger generations are drinking more coffee than older generations so our sample consists of people age 20 to 30.

It was concluded that the participants drink coffee in the morning or afternoon for energy and the caffeine. Most prefer to make coffee at home but some also buy coffee at coffee shops. When asked what kind of coffee they like to drink the most common response was Colombian and all the participants but one cared where the coffee comes from. All participants cared about the flavor of the coffee and this was mentioned several times throughout the interviews. Good coffee according to the participants is dark and strong, made with quality beans, and smooth not bitter. Bad coffee is bitter or burnt coffee, powdered or instant coffee, and weak coffee. The participants also choose their coffee based on the brand and friends but all drink a different brand from Lavazza and Blue Horse to Dunkin Donuts and local coffee. Two of the participants have brand loyalty and almost always buy the same brand while the others usually buy the same brand but don't mind trying new coffees. All the participants said that Brazilian, Colombian, and Ethiopian coffee is good quality coffee, if not the best.

When asked if they would try coffee produced in China, half the participants immediately said yes or why not and half seemed hesitant but most said if it was good coffee they would try it. One participant said they wouldn't try it because they weren't sure about the hygiene having experience living in China. Another mentioned the lack of regulations in China and that would keep them from drinking coffee from China. This lead us to the next question with three interviewees saying they would drink or buy coffee produced in China and three saying no they wouldn't buy it. When asked if they thought others would buy it, most said they didn't think so, or at least not at first. One mentioned the number of fake products in China and was worried that fake coffee could also be made. The interviewees were asked to define Chinese coffee in three words and the most popular response was poor quality followed by cheap. They were then asked to define Nescafe in three words and the most common response was average quality followed by diverse products. All the participants have tried a Nescafe product. The next question was how much should a cup of Chinese coffee cost if a cup from Brazil is \$3, Ethiopian is \$2.90 and Colombian is \$3.20 with most the participants saying \$2.50, one saying \$1.50 and two saying \$2. The last question was would you buy a cup of Chinese coffee if it were cheap and most said yes but clarified that it had to taste good.

The topics that are related to this thesis were defined and ranked from the most general to the most precise. The sample group provided this thesis with several themes such as habits of buying, habits of drinking and consumption, price sensitivity, brand loyalty, and quality sensitivity. This sample group places a high importance on quality as well as taste. This helps guide the next part of the study.

Following the results of a qualitative study, the goal defined for the quantitative study is to measure the acceptability of Chinese coffee to coffee consumers. This study was done after the sample group and the aim was to validate the data collected from the first study. The sample group was six people and this study will use more people to make it more reliable. It was decided to do an online survey due to the lack of time, ease of use for the participant, and the results are still credible and reliable for a serious study. This study used the funnel method starting with general questions and ending with more precise questions.

To go further, the quantitative study sample size with a minimum of 100 was decided to be satisfactory due to several factors. The first being that previous researchers have used 100 people as a sample size in China for coffee drinkers. A previous researcher also did a similar survey that consisted of 117 Chinese people living in Kunming. Second, when calculating a proper sample size due to population the normal operating margin of error is around five percent with a 95 percent level of certainty. Unfortunately, due to the massive amount of people that drink coffee it would be impossible to survey a proper sample size with a five percent margin of error. Lastly, there was a lack of time and willing participants for an expanded sample size. The sample size for this survey was 151 people from various countries both foreign and Chinese nationals and was exclusively online. It was spread through various social media platforms such as Facebook, Twitter, a WordPress blog and WeChat.

This survey was collected and analyzed on surveyrock.com. The participants who answered no to the first question of do you drink coffee were excluded. This left the survey with 132 participants. The demographics of this survey include 37 percent between the ages 26 to 35, 24 percent between 18 and 25, 15 percent between 36 and 45, 17 percent over 55 and 7 percent between 46 and 55. The participants were 25 percent male and 75 percent female. Over three quarter of the participants work with 86 percent working. Over half are not students with only 32 percent being students. This is in line with previous research that suggests that the younger population drinks more coffee. It was surprising however that only 25 percent of the participants were male when previous

researchers and a previous study for this thesis showed a more even number of males and females.

The conclusion of the results of this quantitative study is that the majority of people would not buy Chinese coffee but most of the participants thought that China could produce good quality coffee. The participants of this survey also place a high importance on quality.

| Would you buy coffee produced in China? | Do you think that China the agricultural abilities to produce quality coffee? |
|---|---|
| Yes: 45 % | Yes: 73 % |
| No: 55 % | No: 27 % |

When asked to rank coffee from Brazil, Colombia, China and Ethiopia based on quality from one to four. Brazil received almost equal percentages between two, three and four with 31, 32, and 30 percent respectively. Colombia received a rank of four with 55 percent. China received the highest percentage ranked one with 46 percent. Ethiopia received 43 percent with a rank of three. This concludes that Colombia was ranked as having the best quality coffee, Ethiopia was ranked second, Brazil ranked third and China was ranked fourth. This means that coffee from the known coffee producing countries is perceived to have a better-quality coffee.

When asked what they thought the taste would be a little over half the participants thought that Chinese coffee would be strong, bitter, aromatic and flavorful while disagreeing that it would be smooth and sweet tasting.

Q5. If you tried Chinese coffee what do you think the taste would be?

| | very agree | agree | disagree | very disagree |
|-----------|------------|-------|----------|---------------|
| Strong | 12% | 40% | 40% | 7% |
| Bitter | 10% | 42% | 41% | 7% |
| Smooth | 8% | 38% | 49% | 4% |
| Flavorful | 8% | 55% | 29% | 9% |
| Aromatic | 9% | 44% | 41% | 5% |
| Sweet | 8% | 26% | 55% | 10% |

When asked where would you put Chinese coffee price from very cheap to very expensive, the highest percentage was middle with 43 percent followed by cheap with 37 percent and very cheap at 17 percent. This concludes that most people think that the price

of Chinese coffee with have a cheap or very cheap price with a total of 54 percent. The rest think it will have an average cost.

When asked where would you put Chinese coffee quality from very poor to very good, the highest percentage was poor with 54 percent followed by good with 37 percent, and very poor with 8 percent. This concludes that most people don't think Chinese coffee is good quality with 62 percent saying poor and very poor. This ties into question three to rank which country could produce the best coffee and China being ranked fourth out of the four countries.

The seventh question was where would you put the price of a cup of coffee produced in China knowing that: Brazilian \$3 per cup Colombian \$3.20 per cup Ethiopian \$2.90 per cup? This question received 33 percent at \$2.40 followed by \$2.80 with 30 percent and \$2.60 at 22 percent. The actual price per cup of Chinese coffee was determined to be about \$2.80. The majority of the participants with 55 percent said 20 to 40 cents cheaper than the actual price. Only 30 percent price the Chinese cup of coffee correctly. This gives Chinese coffee a perceived lower price than it actually is. The participants thought that the price of Chinese coffee would be cheap or very cheap in the fifth question regarding price.

Over half of the participants thought that the 18 to 25 age group would be more likely to drink Chinese coffee followed by 36 to 45 with 25 percent and 26 to 35 receiving 23 percent. This ties in with the fact that in China the younger generations drink more coffee than the older generations. As well as worldwide younger people are more likely to drink Chinese coffee.

More than half the participants said that knowing that the coffee quality is lower than other coffees, but the price is also cheaper, they would not buy coffee produced in China with 69 percent saying this. This is a higher percentage than the first question when only 55 percent said they wouldn't buy coffee produced in China. Initially, more people said that they would buy coffee produced in China than at the end of the survey. This could be for a variety of reasons but from the questions in this survey it can be concluded that quality does in fact matter to these coffee consumers. Quality appears to be the number one concern of the coffee drinkers in this survey. This survey asked about price, quality, and taste to determine if coffee consumers would buy Chinese coffee. If the quality of Chinese coffee was good, then it is possible that these people would drink Chinese coffee. It should be noted that little to none of the participants have actually tasted Chinese coffee and this survey is based solely on perception.

6.3 Analysis

The demographics of the survey showed that more of the younger generations took the survey with 61 percent between 18 and 35. This was the target group in the qualitative study as well as supports previous research that the younger generations drink more coffee than the older generations. One third of the participants were also students which also supports this claim. This is good for this study because it is also believed that people from this group are more open to foreign culture and goods so they embrace coffee as part of the western lifestyle. Over 85 percent of the participants are part of the working class which again supports the claim of being open to western lifestyles as well as demonstrating that the middle class and expected middle class have purchasing power and are not as price conscious. There was an uneven ratio of women to men that was surprising. In previous research, the ratio had been almost even compared to this study where three quarters of the participants were female and a quarter were male. That could be attributed to many factors such as it is possible more women use social media or are inclined to participate in an online survey.

The perception of Chinese coffee is, that while at the moment, the quality might not be the same as other coffee producing countries, but it has the ability to produce quality coffee. Initially, when asked about if they would buy coffee produced in China 45 percent said yes and 55 percent said no. At the end of the survey when asked again if they would buy it, knowing that the quality is lower but price is cheaper, 31 percent said yes and 69 percent said no. This is interesting that there is that much difference from the first question to the last. The survey asked questions about price as well as quality and taste which indicated that quality was very important. The qualitative focus group showed that quality and taste were more important than price. In fact, when asked the perceived price a little more than half said Chinese coffee would be cheap or very cheap and the 46 percent said that it would have an average cost. The focus group drinks coffee for the taste and to help wake up and have energy. The participants of both studies have not tasted Yunnan coffee. Therefore, it can be concluded that the quality is more important than taste since quality coffee is perceived to have a better taste than poor quality coffee.

The participants ranked Brazil, Colombia, China and Ethiopia based on the quality of the coffee and the participants ranked Colombia as having the best quality, Ethiopia second, Brazil third and China fourth. Brazil, Colombia and Ethiopia are all very well-known coffee producing countries. These countries have a better perceived quality. China however is not well-known. This could have been a factor as well as many, if not

all, the participants haven't tried Yunnan coffee. It is also possible that they haven't tried coffee from other countries as well. Many bags of coffee list the type of coffee such as Arabica or Robusta and do not specifically list where the beans come from or if the bag does say where the beans come from it is usually on the back of the bag in small print.

The perceived taste of Chinese coffee would be strong, bitter, aromatic and flavorful. This is an interesting combination the participants selected. They disagreed that it would be smooth or sweet. This could be because the participants prefer a stronger coffee over a sweet one or possibly the participants felt that smooth and sweet coffee comes from more experienced coffee growing countries. This overall perceived taste is actually not a bad perception. A strong aromatic and flavorful coffee is good, but bitter is not usually considered good. Overall it is concluded that the taste would not be an issue that would prevent the participants from buying Chinese coffee. The perceived quality was determined to be poor with 54 percent and very poor with 8 percent for a total of 63 percent agreeing that the quality is poor or very poor. When asked to price a cup of Chinese coffee compared to Brazil, Ethiopia, and Colombia China again came in last with the cheapest price. The participants were asked to give the cup of coffee a price based on the prices for the other countries which resulted in 55 percent thinking the cup was 20 to 40 cents cheaper than the actual price. This agrees with the conclusion that quality is the determining factor. Throughout the survey the participants concluded that the quality was lower than other countries and helps to explain why at the end more participants would not buy Chinese coffee.

The results of the quantitative study conclude that the majority of people would not buy Chinese coffee. The participants place a high importance on quality and it can be concluded that quality was the number one concern of the coffee drinkers in this survey. If the quality of Chinese coffee is good and is well-known, then people would drink Chinese coffee. The problem now is that there is little known about the coffee produced in China and its quality. Most people don't know that coffee is grown in China, therefore, it is believed that if more people know about it and this information is spread worldwide then people will be more willing to try and buy Chinese coffee. It is also believed that there should be improvements in quality so that with being more well known, coffee consumers will try and buy coffee produced in China. Chinese coffee farmers and producers have the capability to produce good quality coffee, however the market is still new and young and should be further developed.

The future of the market is very promising. Coffee is growing in popularity every

year within China and there are also more and more foreigners living in China that will buy and drink coffee. The middle class is expected to grow exponentially and with this comes more purchasing power as well as more demand for luxury goods. Coffee is considered a luxury good because of its higher price and that it is considered mostly a foreign good, that only recently started being produced in China. The Chinese consumers embrace foreign goods and the foreign lifestyle as well as their traditional ones. This has led to an increase in demand for such products.

The demand for coffee is also growing which has led to more coffee being imported because Yunnan coffee growers can't keep up with the demand. From this study and research, it is concluded that in the future this market will turn into one of the biggest coffee markets worldwide surpassing other countries with high coffee consumption. It was presented earlier that China is follow a similar pattern to Japan over 50 years ago and this study concludes that it will continue on that path and could surpass the growth that Japan saw.

This provides many opportunities in the coffee market especially for companies such as Nestlé that are already in the coffee business and have been since the beginning. The next chapter talks about Nestlé and its business in China. The company could see a great deal of growth in the next five to ten years with the market following the current pattern and its expected pattern.

7 Conclusions

7.1 Conclusions

After extensive research and an independent study, it is concluded that China's coffee market is an emerging market with great potential but lacks the perceived quality that the consumers are looking for. While although China is traditionally a tea drinking country, Japan and the UK are also traditionally tea drinking countries that have a flourishing coffee market. The future of this market is predicted to become the largest coffee market in the world.

Instant coffee dominates the market which leaves ample room for the fresh brewed coffee market to grow, while also allowing instant coffee to maintain a significant market share. The increases in incomes and the new emerging middle class will lead to an increase in consumption. The consumption habits of Chinese consumers are growing every year, at a rate similar to Japan 50 years ago when coffee was first introduced. If China continues on this path, then China could be the world's largest consumer of coffee. This is true especially due to the increase in incomes, the immense population, and the social status of having a western lifestyle. These three factors attribute to the potential of the Chinese coffee market.

The coffee market is not limited to the consumption of coffee. There is potential for the coffee producers and manufacturers as well. Companies, like Nestlé and Starbucks, have invested heavily in the production of coffee in Yunnan. The coffee farmers are producing more and more coffee beans each year, as well as, more farmers deciding to grow coffee due to the profitability as demonstrated earlier. There is the possibility to expand the amount of land growing coffee in Yunnan but also in the other regions that grow coffee. This would signify that the Chinese coffee farmers could supply the beans for the domestic market. In turn, Nestlé can use those beans in their domestic products to cut costs and promote the development of the Chinese coffee market.

Nestlé was the first to enter the coffee market in China and since then been very profitable. It is believed from this study that Nestlé has heavily invested in coffee in Yunnan, not only because the Chinese government wanted them to have a local supply chain, but also because they wish to use the coffee beans from Yunnan in their domestic products. This is fine for their instant coffee products since most them have cream and/or sugar already added and quality doesn't need to be as high.

However, if Nestlé wants to use Yunnan coffee beans in their freshly brewed products, then Nestlé must work with the farmers to improve quality. Since the market is relatively new compared to more mature markets, the quality of the beans is lower. The quality depends on many things from the variety of coffee beans, the processing method, and drying method. This is important because from the study, it was concluded that the consumers of coffee place a high importance on quality.

7.2 Implications

It is important for not only producers but also retailers to understand the perception of coffee produced in China, especially with the amount of investments and the increases in both production and consumption. This study uses survey data from coffee drinkers from around the world to determine the perception of Chinese coffee. Specifically, to answer the question if both Chinese nationals and foreigners would buy and/or drink coffee produced in China. This study centered on providing an understanding of the Chinese coffee market, Nestlé in China and their future for the Chinese coffee market. Based on the research, this study is the first to look at the perception of coffee produced in China. The study showed that Chinese coffee was perceived to have a lower quality and the majority of the participants would not drink/buy Chinese coffee. However, three-quarters of the participants thought that China has the capability to produce good quality coffee.

Multiple researchers have concluded that the country of origin has little importance to the Chinese consumers. Since Chinese coffee drinkers might prefer foreign coffee due to its presumed better quality but because it is expensive they might buy a cheaper domestic brand. Chinese consumers may want to buy and drink a better-quality coffee. This is good for growers, producers and sellers of coffee in China. If the growers can increase production, then they can sell their goods in the domestic market. This will help develop the domestic market by lowering costs for sellers of coffee by being able to buy locally or domestically and saving the importing, tariffs and shipping costs. It will also help the market because Chinese people are expected to have increasingly higher incomes, so if the Chinese coffee farmers are providing the coffee for the domestic market, then it is expected that as incomes increase more people will buy coffee. This means that they would be buying Chinese coffee from the beginning if the coffee farmers can produce enough coffee. This also means that they will start drinking coffee by drinking Chinese coffee and by doing so, they will be building a loyalty to the brands they drink.

To end, based on the results, the producers and retailers of coffee in China should focus on improving quality. The growing disposable incomes and interest in the western lifestyle is influencing the Chinese consumers. Culturally, the Chinese consumers place importance on quality over price since they think about products in the long term. The perception of Chinese coffee is not well perceived and the majority of consumers would not buy coffee produced in China. Nestlé is already very successful in China, but there is significant room for growth in the brewed products. Nestlé should focus more on this market since the middle class is expected to grow drastically and this market has the most potential. To conclude, it is suggested that Nestlé and other manufacturers invest more in the quality of the coffee beans instead of in the quantity of sales, since quality is valued more than the price, if they want Yunnan coffee to have a place in the world coffee market.

7.3 Limitations and Future Research

While this study provides valuable information about the perception of coffee produced in China, there were limitations to this investigation. There was no previous research found on the perception of Chinese coffee or Nestlé in China. The focus was on consumer trends, Starbucks, and willingness to pay. It is important to note that China is not yet a member of the International Coffee Organization and therefore it is difficult to collect statistics in the coffee sector. This data was collected this year and at a time when not only is Chinese coffee consumption increasing every year, but also the coffee producers are beginning to produce more. Future research on this topic, could attempt to collect more data as well as explain more about the perception of Chinese coffee. Although our sample was deemed to be large enough and a good representation of international and domestic citizens, it is better to have additional data to include a larger sample as well as expand the representation of people around the globe. In the future, research could collect perception data from multiple cities and countries.

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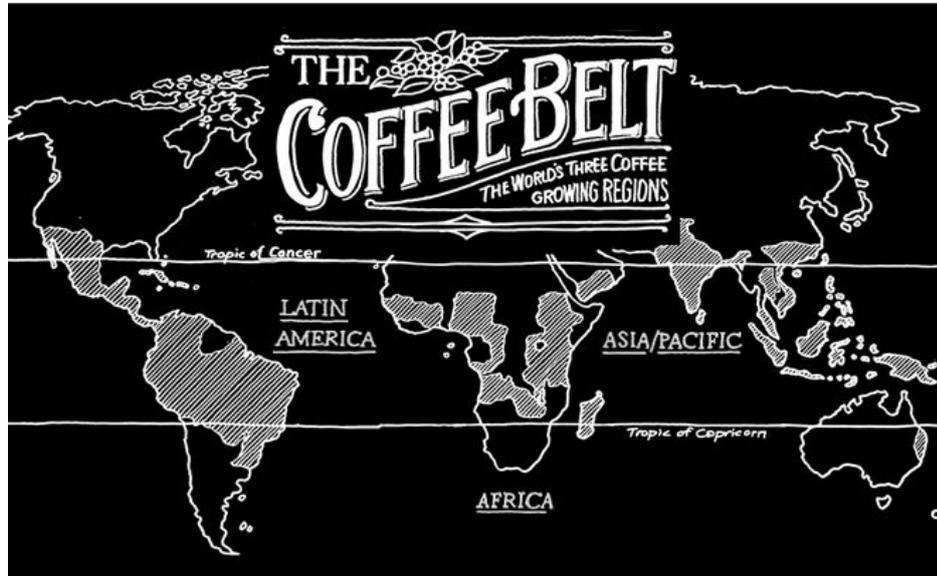
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Appendices

A1: 9 (1) Interesting Facts You Never Knew About Your Coffee! (2016, May 29). Retrieved April 12, 2017, from <https://freshpresso.net/9-1-interesting-facts-you-never-knew-about-your-coffee/>

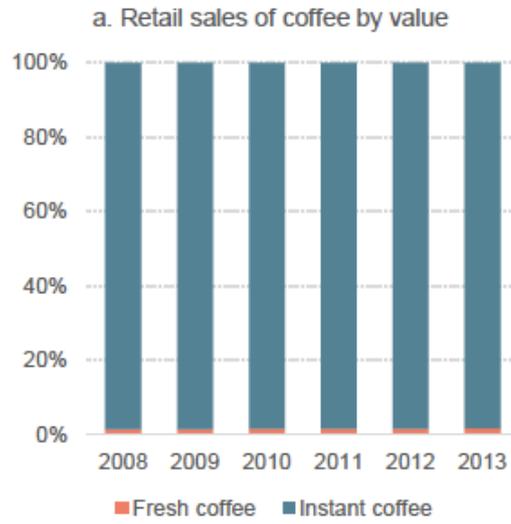


A2: Map of China Provinces. (n.d.). Retrieved April 12, 2017, from <http://www.chinahighlights.com/map/china-provincial-map/>



A3: Coffee in China. (2017, February). Retrieved April 10, 2017, from <http://www.euromonitor.com/coffee-in-china/report>

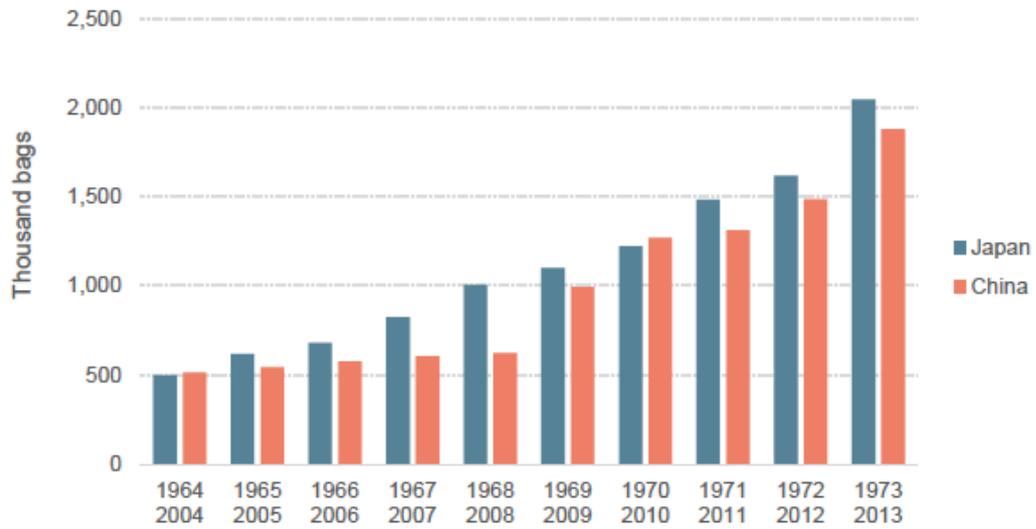
Figure 1: Market composition of retail sales by value



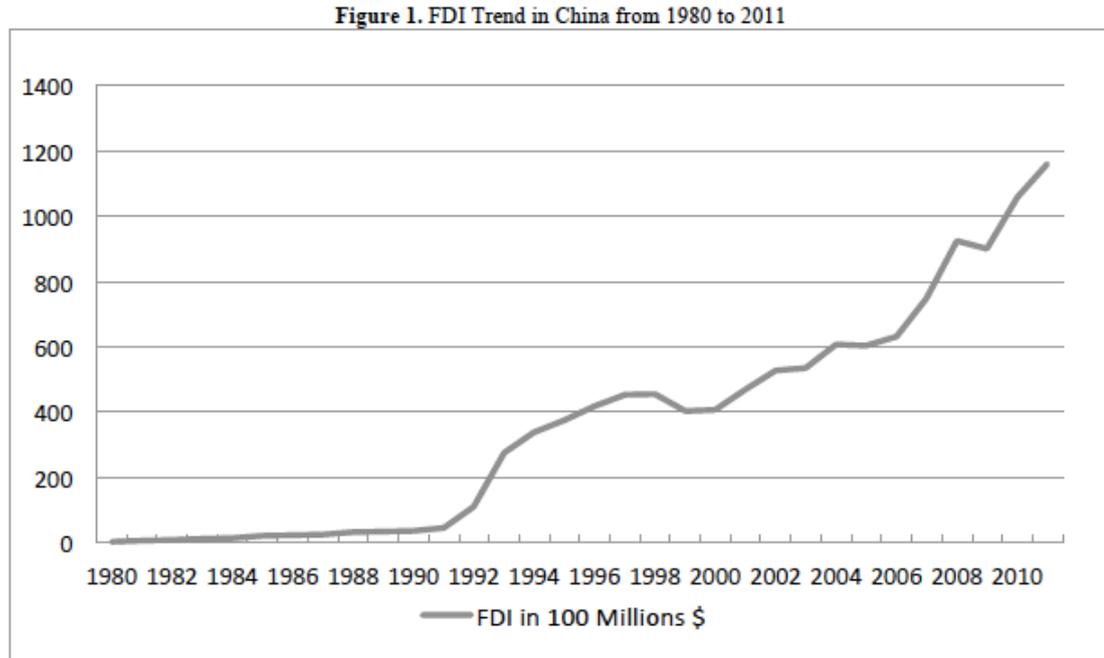
Source: Euromonitor International

A4: International Coffee Organization (2013). Coffee in China.

Figure 5: Coffee consumption in China (2004/05 to 2013/14) compared to Japan (1964/65 to 1973/74)



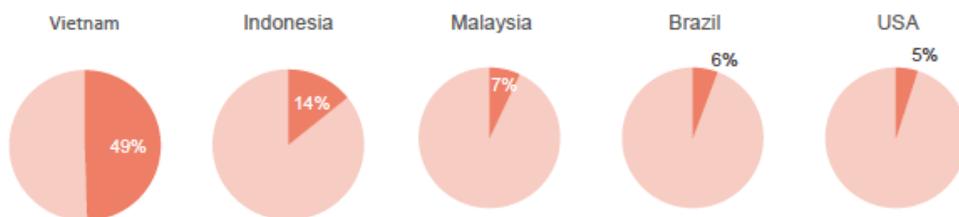
A5: China Statistical Yearbook-2015. (n.d.). Retrieved March 23, 2017, from <http://www.stats.gov.cn/tjsj/ndsj/2015/indexeh.htm>



Source: *China Statistical Yearbook* by China's National Bureau of Statistics

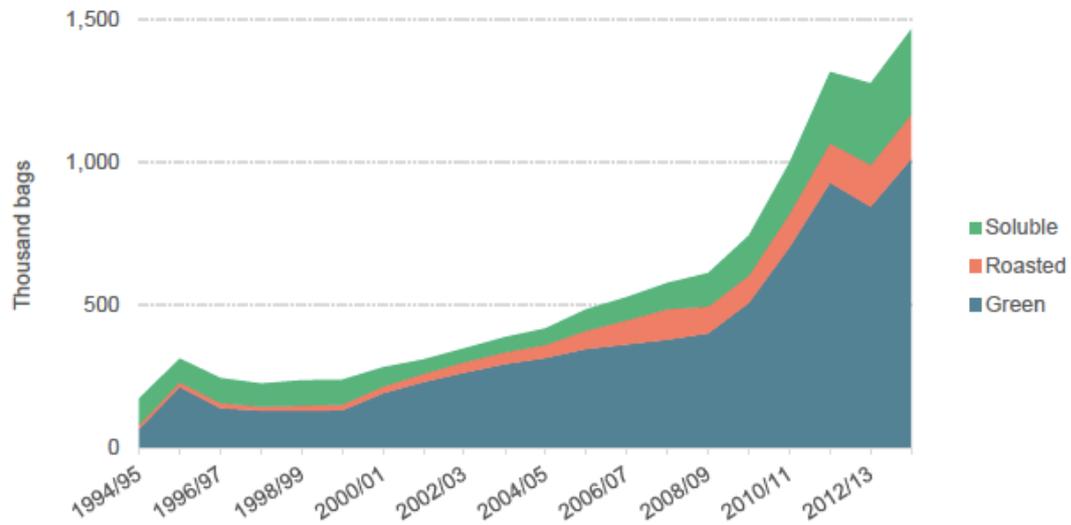
A6: International Coffee Organization (2013). Coffee in China.

Figure 4: Origin of coffee imports by China (Average: 2009/10 to 2013/14)



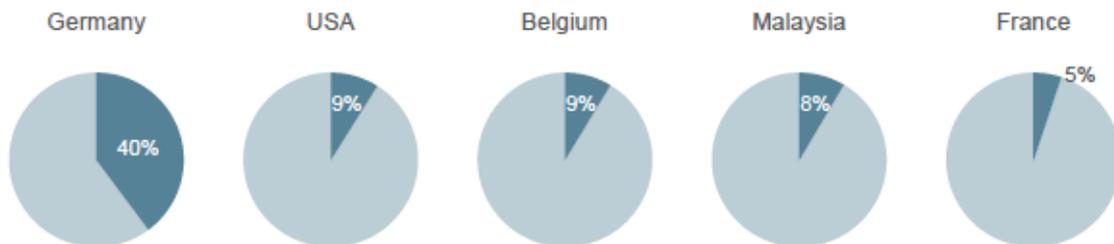
A7: International Coffee Organization (2013). Coffee in China.

Figure 3: Coffee imports by China by form of coffee



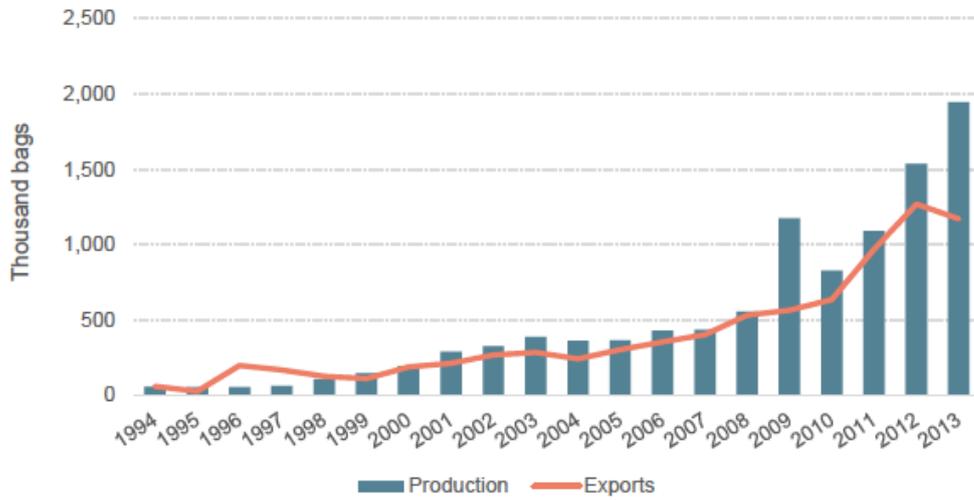
A8: International Coffee Organization (2013). Coffee in China.

Figure 8: Destination of coffee exports by China (Average 2009/10 to 2013/14)



A9: International Coffee Organization (2013). Coffee in China.

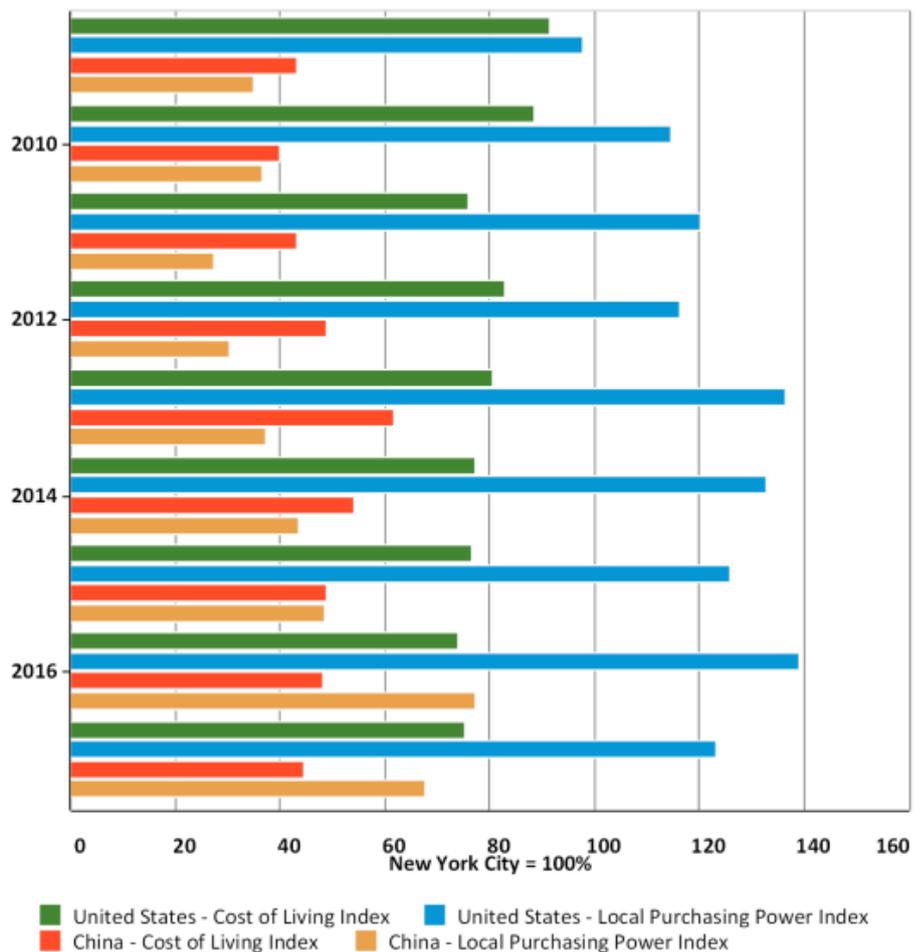
Figure 7: Production and exports in China (1994/95 to 2013/14)



A10: Cost of Living Index by Country, 2017. (n.d.). Retrieved April 12, 2017, from

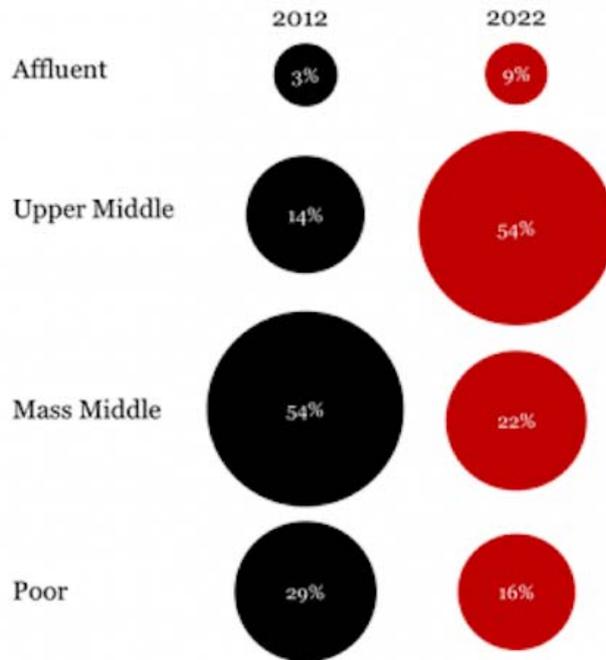
<https://knoema.com/COOFLIIND2016/cost-of-living-index-by-country-2017>

Cost of Living Index by Country, 2017



A11: Barton, D., Jin, A., & Chen, Y. (2013, June). Mapping China's middle class. Retrieved April 10, 2017, from <http://www.mckinsey.com/industries/retail/our-insights/mapping-chinas-middle-class>

China's Middle Class as Percent of Urban Households



Source: McKinsey & Company
Household incomes:
Affluent: >\$34,000
Upper Middle: \$16,000 - \$34,000
Mass Middle: \$9,000 - \$16,000
Poor: <\$9,000

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B1: Qualitative Study

1. Buying and Consumption Habits

- a. Do you often drink coffee?
- b. At what time of the day do you usually drink coffee? (*morning, midday, afternoon...*)
- c. Where do you usually drink coffee? (*at home, at work, at a café, to go...*)
- d. How do you drink your coffee? (*powder, pods, brewed...*)
- e. If I say coffee what comes to mind? (*country, taste, place, time of year...*)
- f. What kind of coffee do you like to drink? (*Brazilian, Ethiopia,...*)
- g. Do you often buy coffee at a café?
- h. Do you care where the coffee comes from when you buy it?

2. Motivations and Objections

- a. What do you prefer when drinking coffee? (*flavor, aroma, caffeine...*)
- b. What do you really dislike about coffee? (*price, flavor...*)
- c. Why do you drink coffee? (*energy, relax...*)
- d. According to you what is a good coffee?
- e. What is a bad coffee?
- f. How do you choose your coffee? (*price, quality, internet, friends, brand...*)
- g. Do you often buy the same coffee or do you like to change?
- h. What brands do you drink?
- i. Do you like to try new coffees?
- j. What do you think of Brazilian coffee? Colombian? Ethiopian?
- k. Would you like to try coffee produced in China?
- l. Would you drink or buy coffee produced in China?
- m. Do you think others would drink or buy coffee produced in China?

3. Ideal Chinese Coffee

I'm working on coffee produced in China specifically Nescafe products in China and I'm working on the requirements for it to be sold and drunk abroad.

- a. Define Chinese coffee in 3 words
- b. Define Nescafe in 3 words
- c. Have you tried it?
- d. How much should a cup cost? Brazilian is \$3 Ethiopian is \$2.90 Colombian is \$3.20
- e. Would you buy it if it were cheap?

B2: Quantitative Study:

Do you drink coffee?

Yes

No

Would you buy coffee produced in China?

Yes

No

Do you think that China has the agricultural abilities to produce quality coffee?

Yes

No

According to you, between Brazil, Colombia, Ethiopia and China who could produce the best coffee ranked from 1 to 4 with 1 being the worst and 4 being the best.

Note you should only choose each number once.

| | 1 | 2 | 3 | 4 |
|----------|----------|----------|----------|----------|
| Brazil | | | | |
| Colombia | | | | |
| China | | | | |
| Ethiopia | | | | |

If you tried Chinese coffee what do you think the taste would be?

| | very agree | agree | disagree | very disagree |
|-----------|-------------------|--------------|-----------------|----------------------|
| Strong | | | | |
| Bitter | | | | |
| Smooth | | | | |
| Flavorful | | | | |
| Aromatic | | | | |
| Sweet | | | | |

Where would you put Chinese coffee price?

very cheap

cheap
middle
expensive
very expensive

Where would you place Chinese coffee quality?

very poor
poor
good
very good

Where would you put the price of a cup of coffee produced in China knowing that:

Brazilian \$3 per cup Colombian \$3.20 per cup Ethiopian \$2.90 per cup

\$2.40
\$2.60
\$2.80
\$3
\$3.20
\$3.40
\$3.60

What age group would be more likely to drink Chinese coffee?

18-25
26-35
36-45

Knowing that the coffee quality is lower than other coffees but the price is also cheaper, would you buy coffee produced in China?

Yes
No

Age?

18-25
26-35
36-45
46-55
55+

Gender?

Male

Female

Do you work?

Yes

No

Are you a student?

Yes

No