

Dow Jones Newswires

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By Caroline Henshaw
Of DOW JONES NEWSWIRES

LONDON (Dow Jones)--The growing interest in Western-style coffee culture among China's urban elite has led beverage retailers to set their sights on a new model: the premium home consumption market.

Several of the world's biggest coffee retailers told Dow Jones Newswires they have already started to develop strategies targeting China's growing interest in drinking coffee at home.

Andrea Illy, chairman and chief executive of illycaffè, said the Italian brand is now seeking to open its first boutique coffee shop to sell coffee, machines and other home appliances after running a successful trial in Shanghai.

To a man who turned a family business based in Trieste, Italy, into a global premium brand, new growth in China will be driven by connoisseurs of Western culture in their 30s, "typically foodies, and art and culture lovers."

"The next step will be to start entering in the homes and families by offering iPerEspresso, which allows Chinese consumer to prepare as good coffee at home," he said. iPerEspresso machines sell for around \$300 on illy's website.

He estimates there are around 50 million consumers drinking one coffee every few days in China, but that could quadruple in size in the next decade. And, while growth will be faster in real terms in the more established coffee shop market, he said proportionally the home market will expand much faster.

"Traditionally home coffee consumption three times higher," he added.

Single-serving coffee machines have become fashionable additions to offices and kitchens in Europe and North America in recent years. Nespresso, the high-end brand belonging to Swiss food giant Nestle first entered China in 2007 and opened its third boutique in Shanghai in August of last year.

Nespresso's market Director in China, Manuel Sancho, declined to give a sales forecast for the region. But he said that "China is a country showing tremendous growth potential" for the brand as they tap into "a growing trend for quality" in the market.

That's not to say that retailers have abandoned plans to pull tea-drinkers through their doors. Many retailers are still hoping China's youth will drive growth in coffee consumption of 15-20% a year by patronizing Western-style outlets.

Starbucks Coffee (SBUX.O) in May announced a deal giving it 100% ownership of the 250 stores it had run with Chinese joint-venture partner Maxim's Caterers Ltd. The world's largest coffee chain said it plans to more-than triple its cafes in mainland China to 1,500 stores by 2015.

"We continue to believe that China will become our second home market outside of the U.S.," said a spokesman for the company in China.

For sure, China's coffee consumption has risen as the country's economy has expanded. A 2009 report by the International Coffee Association said official data indicated annual consumption of 127,000, 60 kilogram bags, but that "other credible sources" estimate this could really be more than 800,000 bags.

One of the major inhibitors to the market, however, is wealth. Although China's economy is expected to grow at over 8% into 2012, the number of people with enough disposable income to buy expensive coffee is still limited.

Jeffrey Young, managing director of analyst Allegra Strategies, said coffee drinking remains a luxury experience for consumers in China. "I think at that country's stage of development its still a very distinctive and Westernized thing to do," he said.

For this reason, he expects consumption will "be led by the out of home market" and remain relatively immune to any economic slowdown as it appeals to only the wealthiest buyers. But, "what you can't ignore is the impact that Nespresso is having in the home market," he added.

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