

The Chinese Tobacco Market and Industry Profile

Intended Uses of Report

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As a Party to the World Health Organization's Framework Convention on Tobacco Control (FCTC) since 2005, China is obligated to adopt and implement effective legislation aimed at reducing tobacco use and tobacco smoke exposure among its citizens.¹ Parties to the FCTC recognize that participation of civil society is essential in achieving the policy objectives contained within the treaty.² The FCTC also acknowledges that "there is a fundamental and irreconcilable conflict between the tobacco industry's interests and public health policy interests."³ Civil society can play an essential role in raising awareness about the tobacco industry – its goals, its size and operation, its strategies to promote its products, and to thwart the adoption and implementation of strong tobacco control policies by gaining influence and credibility with policy makers and the public at large. Accordingly, tobacco control advocates should educate policy makers about the tobacco industry and its deadly products in their campaigns to achieve priority policy initiatives contained within the FCTC.

The tobacco industry is one of the most profitable in the world and the global cigarette market is valued at USD 611 billion.⁴ To market their products, tobacco companies use their enormous wealth and influence both locally and globally. Even as advocacy groups and policy makers work to combat the tobacco industry's influence, tobacco companies and their allies use new and manipulative tactics to circumvent tobacco control efforts. It is important for tobacco control advocates to know who the companies are, how and where they operate, what types and quantities of products they sell, and what kind of marketing tactics they use. This information can help provide advocates with the knowledge they need to expose and counter the tobacco industry and its allies.

Tobacco companies typically report market data annually at least several months after the end of the fiscal year. Therefore, annual market data reported by analysts and tobacco companies are one or two years old. Additionally, while the Chinese tobacco industry makes a lot of data available, it can be difficult to understand and analyze. This report reflects the most recent general trends, forecast data, and tobacco industry positioning within the market that we are able to obtain from government sources, tobacco analysts, Euromonitor International, and other sources.

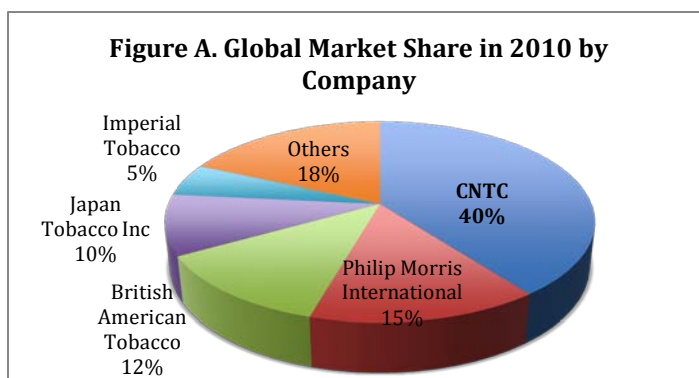
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1. Introduction

The Chinese government plays conflicting roles in China's tobacco sector, as both owner and regulator of the industry. The government is mandated to oversee the growth of the China National Tobacco Corporation (CNTC), the world's single largest producer of cigarettes. At the same time, it has a responsibility to protect public health by reducing tobacco use and tobacco smoke exposure, according to China's obligations under the World Health Organization's Framework Convention on Tobacco Control (FCTC).

CNTC serves the largest domestic tobacco market in the world. In 2010, the company produced 40% of the world's cigarettes (Figure A), or 2.27 trillion sticks.⁵ Most of the cigarettes produced by CNTC are consumed by China's 300 million adult smokers.⁶ In total, more than 50% of adult males smoke while 2.4% of adult females smoke.⁶



China ratified the FCTC in 2005; yet, the retail sales volume of cigarettes grew by almost 23% (from 1.88 trillion sticks to 2.32 trillion sticks) between 2005 and 2010.⁵ In addition, the retail value of China's cigarette market in 2010 was RMB 922.1 billion, or USD 136.2 billion, up 76% from RMB 522.0 billion, or USD 77.1 billion, in 2005.⁷ By comparison, the retail value of the world's next largest cigarette market, Russia, was USD 18.2 billion in 2010.⁸

China has an established smoking population with potential for further growth. Top publicly traded tobacco companies, including Philip Morris International (PMI), British American Tobacco (BAT), Japan Tobacco International (JTI), and Imperial Tobacco, are aggressively seeking to increase their share in the Chinese market. However, the Chinese government keeps a tight rein on the market, not just controlling the production and export of local brands, but also strictly limiting imports and the domestic production of foreign brands.

Currently, less than 1% of the 2.27 trillion cigarettes produced by CNTC is exported each year.⁷ CNTC hopes to increase its share of the global market, in part through strategic partnerships with transnational tobacco companies, such as PMI. The company leverages access to the Chinese market to build such partnerships, giving CNTC more channels to sell their products overseas in emerging markets such as Eastern Europe and Latin America.⁹

Tobacco industry analysts project the continued growth of the Chinese market in both the volume and value of cigarettes sold, despite tobacco control efforts obligated by the FCTC.¹⁰ The volume of cigarettes sold in China is projected to increase by 19% to 2.75 trillion sticks and the retail value by 90.8% to RMB 1,759 billion, or USD 260 billion, between 2010 and 2015.⁵ Chinese tobacco exports are likely to continue to increase as well, as CNTC plans to continue building strategic partnerships and consolidate the tobacco industry in China.

2. History and Major Players

Tobacco Industry Structure

China established the China National Tobacco Corporation (CNTC, 中国国家烟草公司) in 1982 as the business entity of the tobacco monopoly. It established the State Tobacco Monopoly Administration (STMA, 国家烟草专卖局) in 1984 as the government's regulatory arm, both to regulate and to manage development of the tobacco industry. CNTC and STMA are, in effect, one organization with the same leadership and structure.¹¹ The two entities even share one government website (www.tobacco.gov.cn). CNTC is the umbrella company for approximately 30 smaller tobacco companies in China¹² and is "responsible for centralized management of staff, finance, properties, products, supply, distribution, and domestic and foreign trade of the country's tobacco industry."¹³ STMA, in conjunction with CNTC, determines the overall government tobacco policy, including tobacco leaf quotas, pricing, cigarette production quotas, and more, whereas CNTC is considered the implementation arm of STMA policy.⁹

CNTC pays taxes and hands over profits to the Chinese government. In 2011, CNTC handed over RMB 752.96 billion, or USD 119 billion, including RMB 600.12 billion, or USD 94.3 billion, in profits, to the Chinese government.¹⁴

In 2008, the newly established Ministry of Industry and Information Technology (MIIT, 工业和信息化部) took STMA under its jurisdiction, and therefore, indirect control over the tobacco industry.¹⁵ MIIT is considered one of five "super ministries" in China, with responsibilities ranging from industry and trade management, to defense, to technological industrialization.¹⁵ At the same time, MIIT oversees the Inter-Ministerial Coordination Mechanism for Performance of Convention, the inter-agency government body in charge of implementing China's obligations under the FCTC (also known as the FCTC Implementation Coordination Mechanism).¹⁶ The role of MIIT in simultaneously overseeing the regulation of China's tobacco industry and the implementation of FCTC measures represents an inherent conflict of interest, and violates China's obligation to meet FCTC Article 5.3, which requires China to protect tobacco control policies from the vested interest of the tobacco industry.

Industry Consolidation

Over the last decade, China's tobacco industry has been undergoing a major restructuring that includes the consolidation of cigarette producers. The number of cigarette companies under CNTC has dropped from 185 in 2001 to 30 in 2010, while the number of brands has decreased from more than 1,800 to 133 over the same period.^{12,17} CNTC reduced the number of cigarette factories and brands in an effort to create economies of scale and to focus production on a limited number of Chinese brands that could better compete on the international market.¹⁸

3. Domestic Environment

Major Domestic Companies and Brands

China's cigarette market has seen steady increases in terms of both retail sales volume and value. In 2010, 2.32 trillion cigarettes were sold in China and valued at RMB 922 billion, or USD 136 billion.⁵

- The volume of cigarettes sold grew by almost 23% between 2005 and 2010 (from 1.88 trillion sticks to 2.32 trillion) while the retail value grew by 76% (from RMB 522 billion to 922 billion).
- Under CNTC and STMA, about 30 cigarette companies produce more than 130 brands.¹² STMA sets production quotas for both cigarette factories and brands.¹³
- The top five Chinese companies combined produced one trillion cigarettes, or 43.5% of all cigarettes sold in China, in 2010.⁷ The top five cigarette brands sold in China accounted for more than one-fourth (26%) of all cigarettes sold in China (Table 1).⁷

TABLE 1

Top Five Companies by Retail Volume (%)	2006	2007	2008	2009	2010
Hongta Tobacco Group Co Ltd	6.6	10.3	11.0	10.6	11.7
Hongyun Honghe Group	-	-	11.4	9.8	9.4
China Tobacco Hunan Industry Corp	8.0	8.5	8.9	8.9	8.9
China Tobacco Hubei Industry Corp	5.6	6.0	6.3	6.8	6.9
China Tobacco Henan Industry Corp	7.2	7.0	7.4	7.2	6.5
Total	27.5	31.9	45.0	43.4	43.5

Top Five Brands by Retail Volume (%)					
Hongtashan (Hongta Tobacco Group)	1.7	3.0	4.2	4.8	6.2
BaiSha (Hunan Industry Corp)	4.5	5.0	5.7	6.0	5.7
Red Golden Dragon (Hubei Industry Corp)	3.6	4.6	4.6	5.0	5.1
Honghe (Hongyun Honghe Group)	3.6	3.7	4.1	4.5	4.7
Hongqiqiu (Henan Industry Corp)	2.9	3.4	4.2	4.6	4.4
Total	16.4	19.7	22.8	24.8	26.1

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Hongta Tobacco Group Co., Ltd. (Hongta Group)

Hongta Group (红塔集团) is China's leading tobacco company in terms of retail sales volume.¹⁹ Established in 1956 in Yunnan Province as the Yuxi Cigarette Factory, it became the Yuxi Hongta Tobacco Group Co., Ltd in 1995, and is now known as Hongta Group. The company also invests in the financial sector, energy, transportation, and real estate, and engages in other business activities.²⁰



- In 2010, Hongta Group had a retail sales volume of more than 270 billion cigarettes, accounting for 11.7% of all cigarettes sales in China.⁵

- Hongta is the producer of China's best-selling cigarette brand of 2010, *Hongtashan* (紅塔山). The brand had a retail sales volume of 143.7 billion cigarettes in 2012, accounting for more than 6% of all cigarette sales in China.⁷
- Hongta also produces *Hongmei* (紅梅) and *Yuxi* (玉溪) which are the 10th- and 22nd- ranked brands, selling more than 74 billion and 34 billion sticks, respectively, in 2010.⁷
- The company produces *West* cigarettes for distribution in China under a 10-year agreement with Imperial Tobacco signed in 2003.²¹ (See *International Partnerships – Imperial Tobacco*)
- Hongta Group owns companies abroad including Hongta Hong Kong and Hongta Switzerland Ltd., Lao-China Good Luck Tobacco Company, and Hongta Tabaco LatinAmericano.²²
 - Hongta Hong Kong, formally known as Hong Kong Hongta International Tobacco Co Ltd, and Hongta Switzerland Ltd focus on international brand development. The companies target Hongta products toward developing markets such as Africa, the Middle East, and Eastern Europe.²⁰

Website: <http://www.hongta.com/>

Hongyun Honghe Group

Hongyun Honghe Group (紅云紅河烟草集团) is China's second-largest tobacco company in terms of retail sales volume. The company was established in 2008 with the merger of Hongyun Tobacco Group Co., Ltd. and Honghe Cigarette Factory. Hongyun Honghe Group is the biggest tobacco company in China in terms of production facilities, with six manufacturing plants, at least two equity-controlled domestic subsidiaries, and one factory in Myanmar.²³ Hongyun Honghe also invests in trade, printing, logistics, hotels, schools, and hospitals.²³

- In 2010, Hongyun Honghe had a retail sales volume of 218 billion cigarettes, accounting for 9.4% of all cigarette sales in China.⁷
- The company's bestselling brand is *Honghe* (紅河), ranked 4th with almost 110 billion cigarettes sold in 2010.⁷
- Other top brands include *Yunyan* (云烟), ranked 8th with a retail sales volume of 85 billion cigarettes, and *Lesser Panda* (Xiaoxiongmao, 小熊猫), ranked 31st with more than 15 billion sticks sold.⁷



Website: <http://www.hyhhgroup.com/>

China Tobacco Hunan Industrial Co., Ltd.

China Tobacco Hunan Industrial Co. (湖南中烟工业有限责任公司) is the third-largest company in terms of retail sales volume. Established in 2003, it is the only tobacco company in Hunan Province following its acquisition of Changsha Cigarette Factory and Changde Cigarette Factory in 2006. Hunan Industrial Co. also invests in life insurance, transportation, communications, hotels, real estate, and other business ventures.²⁴

- In 2010, Hunan Industrial Co. had a retail sales volume of 206 billion cigarettes, accounting for 8.9% of all cigarette sales in China.⁷

- The company produces the second-top selling brand in China, *BaiSha* (白沙), with a retail sales volume of 131 billion cigarettes in 2010.⁷
- Other top brands include *Furongwang* (芙蓉王), ranked 16th with a retail sales volume of 42 billion cigarettes, and *Furong* (芙蓉) with 33 billion cigarettes in 2010.⁷
- Through a 2008 agreement with PMI, Hunan Industrial Co. produces *Marlboro* cigarettes for domestic sale in its Changsha Cigarette Factory.²⁴ *Marlboro* cigarettes are no longer imported into China. (See *International Partnerships – Philip Morris International*).



Website: <http://www.hngytobacco.com/>

China Tobacco Hubei Industrial Co., Ltd.

China Tobacco Hubei Industrial Co. (湖北中烟工业有限责任公司) is the fourth-largest cigarette company in terms of retail volume. It was formed in 2003 after the merging of the Wuhan Tobacco Company and the Three Gorges Cigarette Factory.

- Hubei Industrial Co. had a retail sales volume of 160 billion cigarettes in 2010, accounting for 6.9% of all cigarette sales in China.⁷
- The company produces *Red Golden Dragon* (Hongjinlong, 红金龙), the third best selling cigarette brand, with a retail sales volume of 117 billion cigarettes in 2010.⁷
- Other top brands by Hubei Industry Co. include *Yellow Crane Tower* (Huanghelo, 黄鹤楼) and *Diamond* (Zuanshi, 钻石).⁷



Website: <http://www.hbtobacco.cn/>

China Tobacco Henan Industrial Co., Ltd.

China Tobacco Henan Industrial Co. (河南中烟工业有限责任公司) is the fifth-largest cigarette company in terms of retail volume. In 2006, three cigarette factories in Henan Province merged and formed Henan Industrial Co.²⁵

- Henan Industrial Co. had a retail sales volume of 151 billion cigarettes in 2010, accounting for 6.5% of all cigarette sales in China.⁷
- The company's bestselling brand is *Hongqiqiu* (红旗渠), ranked 5th with a retail sales volume of 101 billion cigarettes.²⁶



Website: <http://www.hatic.com/>

Shanghai Tobacco Group

Shanghai Tobacco Group (上海烟草集团有限责任公司) is the seventh-largest cigarette company in terms of retail volume. In 2003, Shanghai Tobacco Group absorbed the assets of the Beijing Cigarette Factory, giving the company production facilities China's three largest cities—Beijing, Shanghai, and Tianjin. The company is also the greatest exporter of Chinese cigarettes (See – *Exporting Chinese Cigarettes*).

- Shanghai Tobacco Group had a retail sales volume of 131 billion cigarettes in 2010, accounting for 5.7% of all cigarette sales in China.⁷

- The company’s most notable brands include:
 - *Double Happiness* – a brand identified by STMA to compete on the international market. (See – *CNTC’s Development Strategy*)
 - *Chunghwa* (中华) – consistently ranked in the top five “grade one” cigarette brands.²⁷
 - *Zhongnanhai* – one of China’s most popular “low tar” brands. (See – *Marketing to “Health-concerned” Consumers*)

Major Foreign Companies and Brands in China

CNTC products account for 98% the Chinese market. The leading transnational tobacco companies, BAT, PMI, and JTI, have a small, combined market share of 1% (Table 2).⁷ Three main brands account for the bulk of this market: *555 State Express* (BAT), *Marlboro* (PMI), and *Mild Seven* (JTI).⁷ A limited number of foreign brands are legally produced in China, including *Marlboro* (PMI) and *West* (Imperial). Other foreign brands are subject to import quotas by CNTC and regulated by the China Tobacco International Co., Ltd. an entity under CNTC (See *International Partnerships*).²⁸

Table 2

Top 3 Foreign Cigarette Company Shares - Retail Volume (%)

	2006	2007	2008	2009	2010
BAT	0.5	0.5	0.6	0.6	0.6
PMI	0.1	0.1	0.1	0.2	0.3
JTI	0.1	0.2	0.2	0.1	0.1
Total	0.8	0.8	0.8	0.9	1.0

Top 3 Foreign Cigarette Brand Shares - Retail Volume (%)

555 State Express (BAT)	0.4	0.4	0.5	0.5	0.5
Marlboro (PMI)	0.1	0.1	0.1	0.2	0.3
Mild Seven (JTI)	0.1	0.1	0.1	0.1	0.1
Total	0.6	0.6	0.7	0.8	0.9

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4. International Environment

CNTC is the driving force behind the increases in world cigarette production. In 2010, the top four transnational tobacco companies (i.e. PMI*, BAT, JTI, and Imperial) all recorded drops in cigarette volume.²⁹ However, global cigarette production still increased due to CNTC's 80 billion increase in cigarette stick production for 2010.⁵

CNTC seeks to expand into the international market and compete more effectively against transnational tobacco companies, using three main strategies: 1) the export of cigarettes produced in China; 2) the establishment of factories abroad, and; 3) the licensing of Chinese brands to foreign companies for production and distribution abroad. CNTC has yet to produce a brand that can compete internationally with PMI, BAT, and JTI owned brands such as *Marlboro*, *Winston*, and *Camel*.

Exporting Chinese Cigarettes

CNTC currently exports very few of the cigarettes produced in China. In 2010, CNTC exported more than 19 billion cigarettes, just 1% of total company production.⁷

- The Shanghai Tobacco Group exported 6.4 billion sticks, representing more than 30% of all Chinese cigarettes exported.³⁰ The company exports its brands to at least 56 countries across six continents. Top exported brands include *Chunghwa*, *Double Happiness*, *Zhongnanhai*, and *Golden Deer*.³¹

CNTC Factories Abroad

CNTC and its subsidiary companies own a number of factories outside of China that produce and distribute Chinese cigarettes to targeted regions. For example:

- CNTC owns Sinorama Industry Com SRL in Romania.³² Sinorama produces *Double Horses*, *Dubliss*, and *Golden Monkey* for the European market.³³
- China Tobacco Guangdong Industrial Co., Ltd. owns Viniton (Group) Co., Ltd. in Cambodia. Viniton is one of the largest cigarette companies in Cambodia and produces *Angkor*.³⁴
- Hongta Group owns a controlling stake in Lao-China Hongta Good Luck Tobacco Company in Laos.²⁰
- Hongyun Honghe Group owns Guogan Cigarette Factory in Myanmar through its subsidiary Qujing Cigarette Factory.³⁵

International Partnerships

China's tobacco companies have also entered into a number of partnerships with international tobacco companies, in part to help facilitate their expansion abroad. Transnational companies, in turn, hope such arrangements can help them to expand in the Chinese market. Currently three of the four top transnational tobacco companies, PMI, JTI and Imperial Tobacco, have direct partnerships with CNTC.

* Excluding 2010 acquisitions, PMI volume was down by 2.5%.

Philip Morris International (PMI)

PMI, a United States corporation, is the world's largest publicly traded tobacco company and sells its products in approximately 180 countries.³⁶ PMI views China as the most important market to penetrate due to its growth potential:

“As we look to the future, there are a number of markets that still represent essentially virgin territory for us. China is obviously our largest opportunity but the magnitude of its potential is matched by its complexity and it is currently very difficult to access in a meaningful manner... Our ambition is to become CNTC's key strategic partner and thus be in a position to capture any meaningful opportunity that may arise should state control of the industry ever be relaxed.”³⁷

–Louis Camilleri, PMI's chief executive officer and chairman (2008)

CNTC and Philip Morris International (PMI) in 2005 announced agreements to manufacture and sell Marlboro cigarettes in China and to establish an international joint venture company.³⁸

- Since 2008, *Marlboro* cigarettes, the best-selling cigarette brand in the world, have been produced and distributed in China by CNTC[†] without a formal quota.³⁹
- Prior to in-country production in 2008, *Marlboro* was imported and had a retail volume of nearly 3 million cigarettes in China. Retail sales volume more than doubled to 6.4 million sticks by 2010, accounting for 0.3% of the total market share in China.⁷
- In exchange, PMI agreed to set up a 50-50 joint venture with China Tobacco International Co., Ltd., that would allow China to:
 - a) offer a range of Chinese brands on the global market;
 - b) expand the export of Chinese tobacco products and tobacco materials; and,
 - c) explore additional business opportunities abroad.³⁸

In 2008, the joint venture launched three Chinese heritage brands in six different markets in Central Europe, Eastern Europe and Latin America. The three heritage brands are *RGD* (low-priced segment), *Dubliss* (mid-priced segment), and *Harmony* (premium segment).

- CNTC markets *RGD* (stands for Red Golden Dragon) within the “low-price” segment. It is currently being sold in the Czech Republic, Hungary, Poland, and Slovakia. Following a strong launch in the Czech Republic in 2008, the brand already accounted for 2% of the country's total market share in 2010.⁵ *RGD*'s market share in Hungary, Poland, and Slovakia is negligible.
- Sinoroma Industry Com SRL, a CNTC-owned factory, produces *Dubliss* in Romania.⁴⁰ The brand was launched in 2008 and is sold in Romania, Russia and Ukraine. Its current market share is unknown.
- PMI subsidiary Massalin Particulares SA launched *Harmony* in Argentina in December



[†] *Marlboro* is produced by the Changsha Cigarette Factory under the China Tobacco Hunan Industrial Co.

2008. The brand is being marketed in the “premium price” segment and is priced the same as *Marlboro*. *Harmony* accounted for 0.4% of Argentina's total market share in 2010.⁵

Tobacco industry analysts note that PMI appears to be in the best position among all the major transnational tobacco companies to become a key strategic partner of CNTC.³⁹

British American Tobacco (BAT)

British American Tobacco is the second-largest publicly traded tobacco company after PMI.⁵ While BAT's *555 State Express* has the greatest foreign brand market share,⁷ the company currently does not appear to have any major partnerships with CNTC. In 2004, BAT announced a joint venture that would allow for domestic production and distribution of BAT cigarettes.⁴¹ However, the joint venture with China East Investments Corporation Limited never occurred.⁴² While the joint venture was in final negotiations, Paul Adams, BAT's chief executive, stated:

“We are committed to China for the long term. For us it represents a major growth opportunity whilst contributing to the Chinese Government's excellent efforts to continue developing the performance of the country's tobacco industry.”⁴¹

BAT's past partnerships with CNTC include:

- In 1996, BAT and Guangzhou No. 1 Cigarette Factory entered into a joint venture to develop the *Cocopalms* brand. The joint venture produced and launched a series of *Cocopalms* cigarettes, including *Cocopalms Lights*.⁴³ The status of the joint venture is unknown.
- In 1999, BAT inherited a partnership with CNTC after it merged with Rothmans International.⁴⁴
 - Huaying Tobacco Co., Ltd., formerly Shandong-Rothmans Tobacco Co., produced BAT's *Craven A* for the Chinese market.⁴⁵ BAT withdrew from the joint venture in 2004, due to dissatisfaction over what it viewed as low production quotas set by CNTC.⁴⁶

Japan Tobacco Inc. (JT) and Japan Tobacco International (JTI)

Japan Tobacco is the third-most profitable publicly traded tobacco company following PMI and BAT.⁴⁷ JT manufactures, markets, and sells its products internationally through Japan Tobacco International (JTI), and is also seeking to access the Chinese market:

“[Japan Tobacco Inc. is] open to discuss any alliance with [CNTC] to support their globalization and at the same time we would like to be an inside player in this very important China market in the future.”⁴⁸

–Hiroshi Kimura, President and CEO of Japan Tobacco Inc., 2008

In 2003, JT established its China Division responsible for Japan's duty-free market and retail markets in China, Hong Kong and Macau.^{47,49}

- The two main functions of the division include “the formation of key relationships in the

Chinese market through technical support of the division and other activities, [...] and the marketing of tobacco products.”⁴⁹

- In 2010, JT’s China Division reported sales totaling 3.5 billion cigarettes from its combined Japanese duty-free market and markets in China, Hong Kong and Macau.⁵⁰ The sales volume specific to China is unknown.

JT has a history of partnerships with CNTC. In addition, the company has inherited partnerships from its acquisition of RJ Reynolds in 1999 and Gallaher Group in 2007.⁴⁷ Below is a breakdown of the various partnerships by origin.

- Japan Tobacco via RJ Reynolds:

- In 1986, RJ Reynolds and Xiamen Cigarette Factory established the first joint-venture tobacco company in China, called Huamei Tobacco Co., Ltd. (also known as China-American Tobacco Co., Ltd). Cigarette production began in 1988.^{51, 44} During the 18-year partnership, Huamei produced the foreign brands *Camel* and *Winston* along with local brands, such as *Golden Bridge* (Jinqiao, 金桥).^{45, 44} In 2004, JT withdrew its investment in Huamei.⁵²
- In 1998, Yanji Cigarette Factory, now owned by Jilin Tobacco Industrial Co., began in-country production of *Camel* cigarettes for RJ Reynolds.⁵³



- Japan Tobacco via Gallaher:

- Gallaher has been exporting its *Sobraine* brand cigarettes to China since 1997. Shanghai Tobacco Group (STG) aided Gallaher by distributing *Sobraine* in Shanghai.^{54, 55}
- In 2001, Gallaher introduced STG’s *Chunghwa* cigarettes in the United Kingdom.
- In 2003, Gallaher and STG signed a reciprocal licensing agreement for their respective brands, *Memphis* and *Golden Deer*.⁵⁴
 - Under the agreement, STG produces and distributes JT’s *Memphis* in Shanghai and, in return, JT produces and distributes STG’s *Golden Deer* in Russia.⁵⁴ The companies launched the brands in their respective countries in 2004.
 - The duration of the agreement and current market share of *Memphis* in China is unknown. The market share of *Golden Deer* in Russia is also unknown. However, according to TobaccoChina[‡], *Golden Deer* sold 515 million sticks in Russia during the first quarter of 2011.⁵⁶

- Japan Tobacco:

- In 2000, JT established a joint venture with Shanghai Gaoyang International Tobacco Co. to produce cigarettes from the “*Seven*” brand family.⁴⁴ Shanghai Gaoyang, and its partnership, is now under the Shanghai Tobacco Group.

[‡] TobaccoChina Online is China’s largest internet provider of tobacco information

- In 2003, JT began importing STG's *Zhonghua*, *Double Happiness*, and *Golden Deer* into Japan.⁴⁹

Imperial Tobacco Inc.

Imperial Tobacco is the world's fourth-largest publicly traded tobacco company after PMI, BAT, and JTI.⁵ Imperial Tobacco only entered the Chinese market in the 1990s and does not have a long history with CNTC.⁵⁷ In 2003, Imperial and Hongta Group signed a 10-year licensing and research agreement.²¹ Under the agreement, Hongta produces and distributes Imperial Tobacco's *West* cigarettes within China, and in return, Imperial markets and distributes Hongta's *Hongtashan* brand abroad.⁵⁸

5. Industry Activities

A national law bans tobacco advertising in movies, on television and radio, and in newspapers and magazines. However, CNTC and the top transnational tobacco companies still engage in a wide range of marketing activities to target the world's largest tobacco market. Tobacco companies can advertise their products at point of sale, through sponsored events and branded schools, on billboards, online, and through extensive advertising of affiliated companies with the same names as tobacco brands.⁵⁹

Marketing Tactics

Exploiting Chinese Culture

Tobacco companies brand and market their products using famous Chinese landmarks and icons. In addition, they try to market their products as the perfect gift, exploiting the Chinese gift-giving culture. In China, gift giving is used as a means to establish and maintain relationships.⁶⁰

- *Hongtashan*, the bestselling cigarette brand in China, takes its name from a famous red pagoda in Yuxi, in Yunnan Province. In 2010, the maker, Hongta Group, launched *Hongtashan Gonghexinxi* (红塔山恭贺新禧) as its first product in a new festival series meant to be given during Chinese holidays and special occasions, such as the Chinese New Year.⁶¹ *Gonghexinxi* means “Wish you the best,” and the red pack with an ancient Chinese coin symbolizes luck and prosperity.
- *Chunghwa* (中华), made by Shanghai Tobacco Group, means “China.” The brand uses the iconic image of Tiananmen Gate, the entrance into the Forbidden City. *Chunghwa* is an expensive brand and offers gift packs for special occasions.
- Additional brands that use iconic Chinese names and landmarks include:
 - *Huanghelo* (黄鹤楼), or “Yellow Crane Tower,” is named after a famous tower in China built in the first century. The pack features an image of the tower and flying cranes.



- *Huangguoshu* (黄果树), or “Yellow Fruit Tree,” is named after Huangguoshu Waterfall, one of the largest waterfalls in East Asia.
- *Zhongnanhai* (中南海) is the name of a famous complex adjacent to the Forbidden City, which serves as the headquarters to the Communist Party and State Council.
- Additional images on cigarette brands that are linked to Chinese culture include dragons on *Red Golden Dragon* (Hongjinlong, 红金龙) and *Zhenlong* (真龙) and stone lions on *Shishi* (石狮) and *Xiongshi* (雄狮).

Marketing to “Health-concerned” Consumers

The major transnational tobacco companies have known for decades that “light” and “low-tar” cigarettes are no safer than regular cigarettes.⁶² However, these companies designed such products with the aim of persuading health-concerned smokers to switch cigarette brands rather than quit.⁶³ Keeping with the international trend towards marketing “light” cigarettes, CNTC uses the phrase “low-tar, low-harm” (低焦油低危害) to describe its current development strategy. The phrase also suggests to consumers that Chinese cigarettes are becoming ‘healthier.’ Common marketing practices aimed at health-conscious consumers include using terms such as “light” or “mild,” printing tar levels on the pack, color-coding cigarette packs to suggest “mildness,” and claiming the inclusion of reduced-harm technologies.



- *Zhongnanhai* (中南海) is one of the most-recognizable brands with a “low tar series” marketed to health-concerned consumers. The brand uses the term “lights,” prints tar levels on packs, and uses color-coded packaging. *Zhongnanhai* is available in “Super” 1mg, 1mg, 3mg, 5mg, 5mg “I Era,” 8mg, 8mg Gold, 10mg, “Blue Time,” and “Blue Fashion.” The brand claims to use nano-technology and Chinese herbs to reduce the harms of smoking.⁶⁴
- Other brands that target health-concerned consumers include *Changbaishan* (长白山) which markets both a “low tar series” and cigarettes with ginseng, a plant seen as having medicinal qualities,⁶⁵ and *Septwolves* (七匹狼), which prominently prints tar levels on the top of some packs.⁶⁶

In 2006, STMA issued a policy requiring all cigarettes produced and sold in China to have less than 12 mg of tar, as measured by a smoking machine, by January 1, 2011.⁶⁷ As a result, CNTC and its subsidiary companies have been focusing on “low tar, low harm” cigarettes as a core development strategy. (See *CNTC Prospects and Future Strategy – Research and Development*)

Marketing to Women and Children

Tobacco companies in China, following strategies used by international tobacco companies, use cigarette packaging, added flavors, and targeted marketing campaigns to entice women and children to smoke. The female smoking population in China is still small at 2.4%.⁶⁸ With the goal of expanding this market, many



famous brands have launched versions of their brand specifically targeted at Chinese women.

- *Zhongnanhai* produces *Zhongnanhai “Romantic”* (中南海“浪漫风情”) in pink packaging that contains menthol and “fresh tea mix.”⁶⁴
- *Changbaishan* produces *Changbaishan “Heavenly Melody”* (长白山“天韵”) in packaging with pink, Chinese-style flowers. The actual cigarette has pink paper around the filter portion—a design feature commonly used to mask women’s lipstick stains.⁶⁵
- Both *Lesser Panda* (Xiaoxiongmao, 小熊猫)²³ and *Pride* (Jiaozi, 娇子)⁶⁹ use child-friendly images of pandas on their packaging.



Marketing to young people is necessary to attract new smokers.⁷⁰ Tobacco companies aim to create brand recognition among potential consumers, and one method they use to encourage youth to smoke is the sponsorship of sports and other events.⁷¹⁻⁷³ CNTC and subsidiary companies have taken sponsorship one step further by fiscally sponsoring schools and naming such schools after the tobacco company.⁷⁴

- Every year, STMA sponsors the Sunflower Cup (太阳花杯活动), an event that engages youth in a variety of educational, artistic, and music competitions in the name of discouraging youth smoking. The Sunflower Cup also has a charity component that invests in youth development.⁷⁵
- Tobacco companies reportedly sponsor more than 100 elementary schools across China, with many of the schools bearing the names of the tobacco companies.⁷⁴ Schools with Chinese tobacco company names include *Zhongnanhai Heart Elementary School* (中南海爱心学校) and *Sichuan Tobacco Hope School* (四川烟草希望学校), which school slogan is “Talent comes from hard work- Tobacco helps you become talented.”⁷⁴



Brand-stretching

To get around tobacco advertising restrictions and create brand recognition, tobacco companies set up foundations and other service companies, and sponsors non-tobacco-related events, using the names of their companies or brands.

- Hongta Group is the manufacturer of the top-selling brand in China, *Hongtashan*. The company sponsors cycling races and teams, such as the “*Hongta Cup*” *Tour of Hainan Island Cycling Race 2008* and the *Yunnan Hongtashan Mountain Bike Team*.⁷⁶
- China Tobacco Fujian Industry Corp. produces the 11th top selling cigarette brand, *Septwolves*. The brand name and logo was extended to create the popular *Septwolves* clothing store.

Corporate Social Responsibility

Tobacco companies use “corporate social responsibility” contributions to try to increase goodwill among policymakers and the public, counter tobacco control efforts, and get around tobacco advertising bans.⁷⁷ CNTC is no exception. According to their website, CNTC engages in poverty reduction, invests in environmental sustainability, donates to education, and provides funding for disaster relief, among other things.⁷⁸ Some of the projects and causes include:

- Poverty reduction and health – supporting economic development plans in poor villages, clean water projects, and providing medical equipment and drugs
- Environment – “Green Yangtze River in Chongqing” Campaign, “Gold Leaf Eco Fund,” tree planting for carbon credits
- Education – “Project Hope,” “Gold Leaf” libraries, “Dream Campaign” (school scholarships)
- Disaster relief – donations to the Red Cross, Yunnan earthquake victims, drought relief in Kunming

Transnational Companies Networking in China

Given China’s monopoly over the tobacco industry, transnational tobacco companies establish relationships and build goodwill with influential Chinese entities as another way to gain access to the Chinese market.

Philip Morris International (PMI)

PMI appointed Baidu CFO, Jennifer Li, to its board of directors in 2010.³⁶ Baidu is the largest Internet search engine in China. International tobacco industry analysts stated that the appointment signals that: “PMI are (sic) hoping the new board member might be a ‘bridge’ to China.”⁷⁹ Nearly twenty years ago, in 1993, Philip Morris International’s leadership recognized the importance of making contacts within China in order to build its business: “The other ‘China lesson learned’ that we see everywhere is that you need the right contacts inside China to get things done...”⁸⁰

British American Tobacco (BAT)

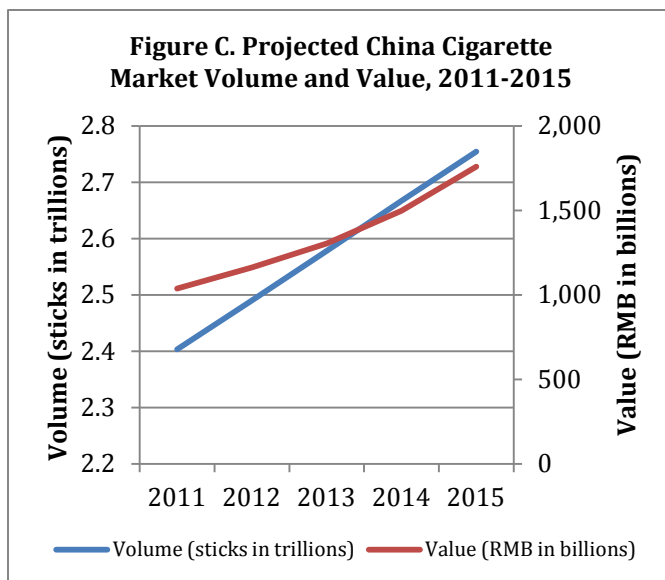
BAT has funded the Beijing Liver Foundation (renamed the Beijing Health Promotion Society in 1999) since 1997 in an apparent bid to divert attention away from secondhand smoke and toward liver disease prevention. In addition, BAT has helped promote the establishment of ventilation and air filtration systems in China as an alternative to 100% smoke-free policies, a practice known by BAT to be ineffective at eliminating the harms of secondhand smoke. It has also offered training to the STMA and Chinese journalists on BAT’s corporate messages, which seek to downplay the harms of secondhand smoke. BAT used the Beijing Liver Foundation to foster a relationship with CNTC/STMA and help them circumvent and undermine smoke-free legislation in China.⁸¹

6. CNTC Prospects and Future Strategy

Future Outlook

Tobacco industry analysts project continued growth over the next few years in both cigarette volume and value in China, despite the potential for future tobacco control efforts as obligated by the FCTC.¹⁰

- By 2015, the volume of cigarettes sold in China is projected to increase by 19% to 2.75 trillion sticks and the value by 90.8% to RMB 1,759 billion, or USD 260 billion.⁵ It is predicted that by the year 2050, China will account for half the world's cigarette market.⁸²
- In 2011, the Chinese government approved its 12th Five-Year Plan (2011- 2015), which for the first time called for comprehensively promoting a ban on smoking in public places. However, industry analysts project that the tobacco control policies will not significantly affect the country's tobacco market over the next five years due to a lack of commitment to enforcement.⁷ Tobacco control advocates note that China continues to fall short in implementing tobacco control measures and meeting its FCTC obligations.⁸³



CNTC's Development Strategy

CNTC continues to restructure and centralize China's tobacco industry. In 2009, CNTC drew up a list of 30 flagship brands. Brands not on the list were required to stop or reduce their production of cigarettes. The next phase of CNTC's development strategy is to create leading brands within the 30 flagship brands through its "532" and "461" plans.⁸⁴

"532" and "461" Plans

In 2010, STMA announced its five-year "532" and "461" strategy for CNTC to become more competitive internationally and generate more revenue.²⁷ Under the "532" plan, the company aims to develop²⁷:

- *Two* brands that would produce more than *five* million cases, or 50 billion sticks, per year.
- *Three* brands that would produce more than *three* million cases, or 30 billion sticks, per year.
- *Five* brands that would produce more than *two* million cases, 20 billion sticks, per year.

Under the "461" plan, STMA hopes to develop 12 brands with a retail sales value of more than RMB 40 billion per year (USD 6.3 billion), including²⁷:

- Six brands with a retail sales value of more than RMB 60 billion each per year.

- One brand with a retail sales value of more than RMB 100 billion per year.

According to tobacco industry analysts, CNTC's goal to develop *Hongtashan* and *Double Happiness* to sell 50 billion sticks each by 2015 is ambitious given current production.⁸⁵ In 2010, *Hongtashan* sold 21.7 billion sticks and *Double Happiness* 16.4 billion sticks.⁸⁵

Research and Development

Another major cornerstone of STMA's future strategy includes the research and development of 'less harmful' cigarettes. STMA's Tobacco Research Institute and its many affiliates conduct extensive research to develop new products and enhance current products to compete in the international market. In fact, the number of research projects on less harmful and low-tar cigarettes grew from 1% in 1983–1987 to 4% in 2003–2007.⁸⁶



- After a 2008 study done by the Tobacco Research Institute of CNTC Shanghai which developed a hazard index of mainstream cigarette smoke, STMA release a list of the seven most harmful chemicals that cigarette manufactures should focus on reducing. Product development centered around the STMA's list included filter technologies which claim to reduce the presence of chemicals such as carbon monoxide and hydrogen cyanide.⁸⁷
- In 2010, STMA announced intentions to double the sale of 'low tar' cigarettes to 80 billion cigarettes in 2011, requiring tobacco companies to rapidly develop and/or produce more 'low tar' cigarettes. During the first quarter of 2011, STMA approved 15 new 'low tar' cigarette products.⁸⁸
- In 2010, Hongyun Honghe Group launched Yunyan 5mg Impression (云烟“5mg 印象”) which claims to have '5mg of tar' and is flavored with blackberry and cherry squash.⁷
- In 2011, China Kangtai Cactus Biotech Inc. launched a new cigarette that blends cactus with tobacco. The cigarettes claim to have lower nicotine and tar levels than other tobacco-based cigarettes on the Chinese market.⁸⁹
- In 2011, Hongta Group launched Yuxi “Manor” (玉溪 “庄园”), China's first 'organic' cigarette. The brand is said to feature organic tobacco and environmentally friendly cigarette paper. Yuxi “Manor” is being marketed as a reduced-harm, high-end cigarette.⁹⁰

7. Conclusion

Cigarette sales in China account for the majority of cigarettes sold globally, and the Chinese tobacco market is projected to continue growing over the next 5 years. Given the size and potential of the Chinese tobacco market, transnational tobacco companies are constantly looking for ways to broaden their access to it and to strengthen their presence in China. CNTC, meanwhile, is attempting to expand its reach internationally by developing and promoting a few Chinese brands, such as *Hongtashan* and *Double Happiness*, that can compete with global market leaders like *Marlboro*.²⁹

With a government committed to expanding the tobacco industry, tobacco industry analysts project that China's market will continue growing over the next five years despite increasing tobacco control efforts. Strong tobacco control policies will be critical to prevent future deaths caused in part by CNTC's dominance of the Chinese tobacco market and its expansion into the global market.

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