

# Food and beverages - [Russia]

Summary of findings related to international market opportunities for Norwegian food and beverage products to Russia

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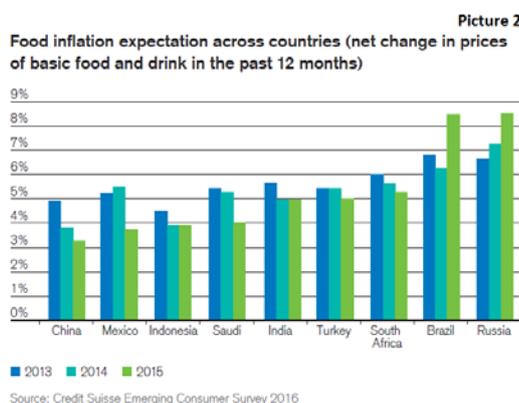
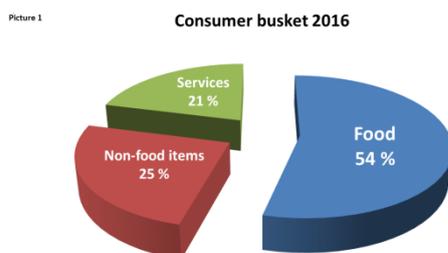
- **Brief facts about the market**

Russia with its 143 mln people population is one of the biggest consumer markets in Europe, consuming foodstuff for about 140 bln USD. Main market groups like alcohol, cigarettes, meat, milk products, confectionary, fruits& vegetables altogether occupy 50% of the consumer market.

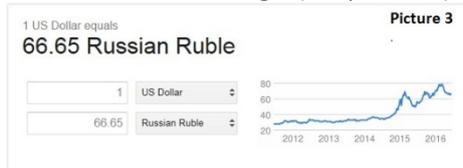
Moscow along with Moscow region (>20 mln people), St. Petersburg along with Leningrad region (7 mln) with their large population are crucial cities for traders but don't forget about other Russian regions, which are increasing purchasing power.

In recent not stable situation when real income of ordinary citizens is falling, more than 80 % of the population have experienced a decrease in living standards, which has consequently resulted in a reduction of consumer activity. Both low-income and medium-income classes have begun to economize. The poverty level is growing (it's now 13,4%). People in Russia become more careful about their cash expenditures and look for ways to save money. Besides buying food, Russians must make monthly payments to cover their debts, mortgages and other financial commitments. In such cases the majority of Russians stop buying cars, expensive electronics, furniture, etc.

However, the family budget for foodstuff and basic goods is always a priority and it's logical when during the crises it has the tendency to occupy the biggest share of Household expenditures. Nowadays 54% of family income is spent for food (+6% from 2014) *see picture 1*



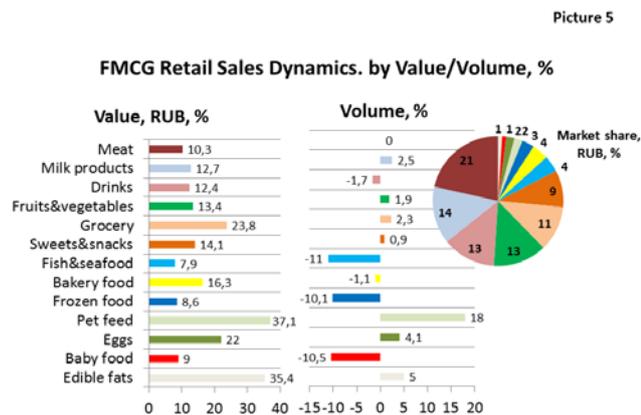
In comparison with other countries Russia is experiencing the highest food and beverage inflation (see picture 2). High currency rate is effectively transmitted to the consumer via import inflation which is influencing every Russian household budget (see picture 3)



Another point is **food embargo** initiated by Russian government in 2014 and prolonged until 2017, which influenced the increase of retail prices and thus increased the food basket budget more than 31%, which is actually more than official inflation rate in the country. (see retail prices 2016 for essential foodstuff in Picture 4)

Picture 4

Essential food items	Average price, \$	Price range
Milk (regular) (1 liter)	0.80	0.63-0.98
Loaf of Fresh White Bread (500g)	0.45	0.34-0.63
Rice (white) (1kg)	0.93	0.71-1.21
Eggs (12)	1.06	0.89-1.25
Local Cheese (1kg)	5.93	4.57-7.73
Chicken Breasts (Boneless, Skinless) (1kg)	3.48	2.79-4.10
Beef Round (1kg) (for equivalent back leg red meat)	6.16	4.95-7.74
Apples (1kg)	1.24	0.93-1.56
Banana (1kg)	0.99	0.79-1.23
Oranges (1kg)	1.27	0.93-1.72
Tomato (1kg)	1.50	1.25-2.69
Potato (1kg)	0.44	0.29-0.67
Onion (1kg)	0.42	0.30-0.60
Lettuce (1head)	0.87	0.60-1.40
Water (1.5 liter bottle)	0.55	0.39-0.77
Bottle of Wine (Mid Range)	6.00	4.56-8.54
Domestic Beer (0.5 liter bottle)	0.84	0.69-1.05
Imported Beer (0.33 liter bottle)	1.63	1.17-2.23
Pack of Cigarettes (Marlboro)	1.47	1.25-1.70



Consumers are cutting food budget after all the others, but prefer to purchase promotional, discounted, private label products as they are cheaper than others. Therefore, sales of Promotion foodstuff grew 35%. Discounted food sales increased 45% in volume. FMCG market segment is the most stable in Russia in downturn economic situation.

Recent average household food budget is allocated as follows: 31% goes for meat, 15% for milk products, 15% for bakery, 10% for fruits & vegetables, 29% for other products.

Consumption per capita/annum: 263 kg milk and milk products, Bakery -99 kg, vegetables & melons– 98 kg, fruits and berries – 71 kg, meat & meat products – 81 kg, Potato – 64kg

Consumer preferences have changed accordingly (see picture 5). It's very big contrast between the perceptions among richest and poorest consumers. Appetites for high quality products and luxury brands in Russia remained undimmed. High income consumers and still stable middle class are reliant on import: certain types of alcohol, bovine meat, fruits and vegetables, ingredients, vitamins, raw materials for processing sector, etc, as local food production is often poor quality and insufficient.

However, the average mass market consumer preferences shows that:

- Ready food became less demanded
- Sauces became more popular (+7% sales increase)
- Milk and milk products (sales increased 15%)
- Spices, canned vegetables (sales increased 117%)
- Pet food (sales increase 18% in volumes)
- Eggs, flour, ingredients for bakery became more popular as families started more to eat home prepared food.

Reputation of a Country of origin is still important for almost all consumers especially in the following groups:

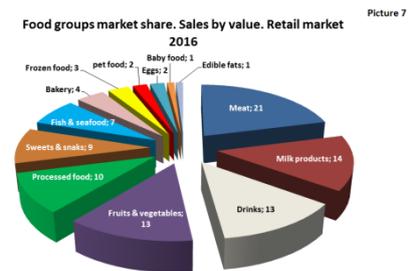
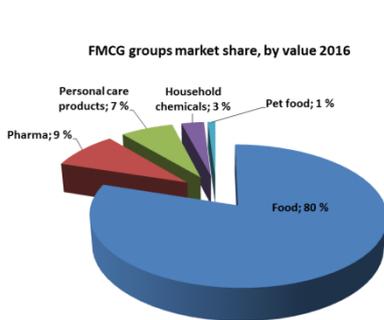
- Chocolate (for 48% respondents)

- Beer and other alcohol (for 52% respondents)
- Cheese, cottage cheese, milk products ( for 25% respondents)
- Fruits fresh, frozen or dried (for 26% respondents)
- Tea, coffee ( for 63% respondents)

Norway as a country of origin is respectable among Russian consumers.

However, Price of food is the priority now! Russians transferred their preferences recently on cheaper and high-calorie products. The interest switched from chocolate to biscuits, from beef – to poultry meat. The share of bakery products grew dramatically.

Russian retail share in Russian trade market reached 66%. The year 2015 brought the biggest growth rate to FMCG segment on the retail market in Russia. The number of shops belonged to Top-10 retail chains grew in average 24,5% per annum. Retail Sales volumes increased 12,5%.



## • Opportunities for Norwegian companies in Russia

Due to active Food embargo initiated by Russian Government, several groups of food products are closed for import from Norway to Russia (*see attachment 1*). However, there are still few food segments having potential for export from Norway to Russia (*see attachment 2*).

The most significant areas of opportunities for Norwegian food and beverage producers are probably:

- ✓ **Food ingredients market**, 3 bln USD size, one of the most dynamically developing nowadays, where foreign manufacturers keep 85% of the market. Hydrocolloids and new kinds of stabilizers are in a big demand by food processing industry in Russia. There is an increase interest to high-quality, natural and environment friendly ingredients. Norway is represented within entire segment only by Borregaard Ingredients supplying vanillin and food fiber SenSefi (microcrystalline cellulose) to food processing sector. Food ingredients market is far from being saturated and having still no limitation by the Russian food authorities.
- ✓ **Alcohol segment** has been always interesting for foreign suppliers because of huge consumption (17 l per capita annually). Especially nowadays the market could be more interesting for foreign suppliers due to State regulations, which lead to increased excise tax up to 30% per, which lead to the 20% increase of retail prices annually. So, such regulatory measures are in the disfavor of the local producers of beer, for example, which previously occupied biggest market share providing lower prices, than foreign suppliers. In connection with the general increase in average price level in the alcohol sector the price difference between local vodka and imported alcohol decreases. Premium alcohol market increased more than 10%.
- ✓ **Confectionary and chocolate market**, showing positive dynamics, stable and predictable, which consumption is close to Europe (6 kg against 8 kg per capita in Europe) highly consolidated, having a trend of “functional confectionery” segment growth.
- ✓ **Pet food market**, the one which is showing stable growth 10% year by year in spite of the economic downturn. Russian consumers never cut down expenses for children and pets!! Recent size of the

market is 2 bln USD. 64% of cats and 26% of dogs in Russia (there are about 30 mln cats and 20 mln dogs registered in Russia) are use ready to eat pet food. Market is dominated (65%) by two biggest market leaders Mars and Nestle, which are followed by other brands including imported, private labels.

- **Challenges for Norwegian companies in Russia**

- ✓ The biggest challenge for the Norwegian companies nowadays is a Food embargo, which was decreed in August 2014 and concerned the biggest part of the export to Russia from Norway – fish & seafood (*see attachment 1*). Food embargo reduced import of foodstuff by 40% to \$26.5 billion from two years ago, according to government data.

Food import restrictions are prolonged by the Russian government until 2017. The ban covers the list of specific products of several sectors: Vegetables and fruits, except prepared vegetables and fruits; Milk, dairy products (notably cheese, skimmed-milk powder, butter, whey powder, fresh products, whole-milk powder, condensed milk), and some processed food containing milk components; meat of bovine animals, pork and poultry ( fresh, chilled or frozen), as well as meat salted, in brine, dried or smoked, sausages and similar products.

However, later on Lactose-free dairy products and baby food, sport nutrition, baby food, beef, poultry and vegetables for baby food production only, which were removed from the restricted list in 2014, from now on are allowed be imported into the Russian Federation. The only thing is that Russian importers will have to prove that products entering Russia are intended for children’s consumption. Russia’s Ministry of Agriculture has been set the task of developing methods of approvals of these consignments. The Ministry will also determine the acceptable volumes (quota) of imported products that are no longer effected by the food ban.

The following items were excluded from the ban: seed materials (potatoes, peas, hybrid sweet corn, onion), biologically active additives, vitamins and minerals designed to compensate for the lack of vitamins and minerals in the human body, flavors, protein concentrates and their mixtures, fiber supplements, food additives, and lactose-free dairy products. Atlantic and trout smolt is also excluded from the list. This will ensure that there is an available capacity for commercial fish farming. Domestic production of smolt now can cover no more than 5% of the existing needs of commercial fisheries. (see attachment 1 and 2).

Following Western sanctions and Russia’s food embargo two years ago, Russia is pursuing a policy of import substitution which is aimed to boost domestic agriculture.

- ✓ Conducting business may be interfered by: complicated regulatory regimes; inadequate IPR protection and enforcement; extensive corruption and inadequate rule of law; inconsistent application of laws and regulations; lack of transparency; and the continued presence of large state-owned or controlled enterprises in strategic sectors of the economy.
- ✓ Food of animal origin products (dairy, meat, fish and seafood etc.) needs certification from the Federal Service for Veterinary and Phytosanitary Surveillance and it is a subject to veterinary control at the Russian state border and on transport. State limitation and quotation could be an obstacle for Norwegian companies-new comers to the market on the initial stage.

- **Recommendations to Norwegian companies considering export of food and beverages to Russia**

- ✓ Successful selling goods in Russia requires adaptation to its commercial climate and business practices;
- ✓ Market research is required to identify opportunities and potential Russian business partners;
- ✓ The choice of a partner/importer is important and should be done only after conducting sufficient due diligence to determine its reputation and reliability;
- ✓ Partners can assist with required testing and certification, customs clearance, warehousing and preparation of Russian-language marketing and instruction materials.

- ✓ Travel to Russia is strongly recommended to establish and maintain relationships with business partners and to understand the market attributes;
- ✓ Business planning should include advertising, market promotion and regular visits to Russia.
- ✓ Marketing in Russia requires patience: exporters should maintain a long-term perspective and not expect immediate results;
- ✓ It's highly recommended to keep a Network with companies already in the market as well as with profiled sector associations, such as Fish Union, Russian Meat Union, Milk Union etc. Non-commercial Associations help to build an effective dialogue between certain business sectors and public authorities, to lobby the adoption of adequate solutions for business which further create favorable conditions for business.
- ✓ Business should always be conducted in compliance with all Russian laws and regulations (taxes, customs, labor, etc.), as well as applicable Norwegian laws and standard business practices.
- ✓ Exporters should avoid selling on open account until they have developed a well-established track record with partner; letters of credit and other secure financing instruments are available. Advance payment from a Russian customer may be the best solution to follow until both parties establish a positive record of payment.
- ✓ Russian importers are attracted to bargains. Norwegian companies exporting to Russia should be prepared to offer competitive prices for their goods facing competition with Asian and other third-country pricing.
- ✓ Imports into Russia are subject to VAT, which is assessed on the CIF value of an imported shipment plus applicable duty.
- ✓ Value Added Tax (VAT) is applied to any product that is imported to Russia, varying from 5% to 18% depending on the products customs classification.