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# GAIN Report

Global Agricultural Information Network

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## Russian Federation

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### Food Processing Sector

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**Report Highlights:**

Russia's stagnating economy has been the key factor affecting the domestic food market. The Russian Government has made import substitution and development of domestic agricultural production a national priority. The food processing sector has garnered special attention by the Russian Government in recent years which implements special supporting programs to improve the efficiency of enterprises, provides diversification of production and improves the competitiveness of manufactured products. In 2014, the industry's output reached 4.68 trillion rubles (\$123.37 billion). However, the food processing sector lacks raw materials due to the current food import ban introduced by Russian Government in August 2014 that pushed manufacturers to switch to alternative foreign suppliers or to locally produced raw materials

## **General Information:**

### **SECTION I: MARKET SUMMARY**

The current development of Russia's food processing sector is influenced by an economic slowdown in the country and uncertain political and economic environment. On August 7, 2014, Russian President Vladimir Putin signed a decree banning a long list of agricultural products from the United States, Canada, European Union, Australia, and Norway as a result of the implementation of economic sanctions against Russia due to events in the region. The list includes red meat, poultry, fruits, vegetables, dairy products, tree nuts, pulses, and many other commodities. Later in June 2015, President Putin signed the decree extending Russia's food import ban until August 5, 2016. Russia is one of the world's largest food-importing countries having purchased more than \$40 billion worth of food, beverages, and agricultural products in 2013. Some food processors purchase more than 70 percent of raw materials for manufacturing food products from abroad before the food ban went into place. In 2014, Russian imports of foodstuff contracted by 8 percent to \$39.7 billion. Lack of raw materials pushed manufacturers to switch to alternative foreign suppliers or substitute the traditional ingredients by locally produced raw materials. The ban on many foreign food products from EU and U.S. manufacturers presents a major opportunity for the domestic manufacturing base. The Russian Government has made import substitution and development of domestic agricultural production a national priority.

Russia recorded its weakest economic growth in 2014 (0.6 percent compared to 1.3 percent in 2013) during any year since the end of the economic crisis in 2008. Experts have identified several reasons for the economic slowdown including a complex geopolitical situation and economic sanctions, the negative investment environment, weaker consumer demand, high interest rates and rising inflation.

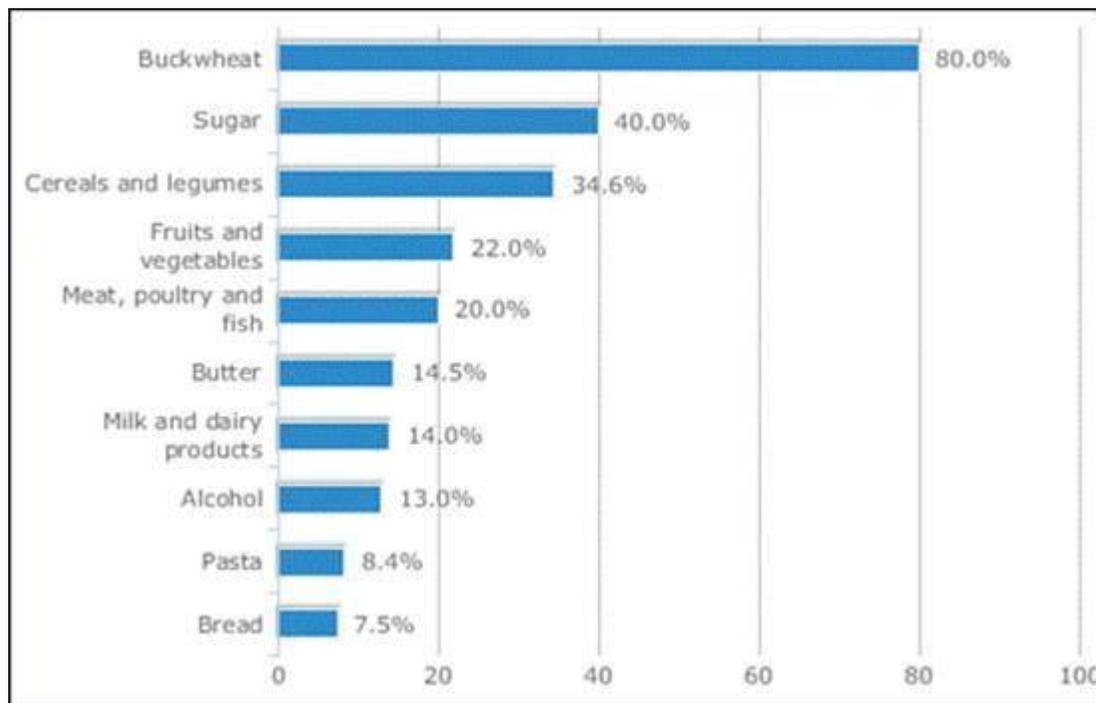
The economic sanctions that the West applied to Russia due to Ukraine crisis exaggerated already harsh credit conditions, banned Russian banks from issuing long-term debt and equity in European and U.S. markets, and limited consumer purchasing power.

The Ruble devaluation against the U.S. Dollar and Euro is one of the factors influencing the industry.

In 2014, the Russian ruble depreciated 70 percent to the U.S. dollar. That same year, the average nominal exchange rate per U.S. dollar was equal to 37.97 rubles; on December 19, 2015, the exchange rate reached 71.32 rubles. The weak ruble presents a key downside risk to household spending as goods become more expensive, pushing down key indicators such as food retail sales value growth in the process.

According to the Russian Federal Statistics Service (Rosstat), consumer price inflation in 2014 rose by 11.4 percent in 2014 – the highest level seen since the financial crisis of 2008 when consumer prices grew by 13.3 percent. Food prices (excluding fruit and vegetables) grew by 14.7 percent in 2014 according to Rosstat data. Retail prices for food items covered by the food import ban surged by an average of 17.9 percent by the end of 2014 after the food import ban was introduced. Cheese, fish, and meat prices rose the fastest as a large percentage of these products have historically been imported from overseas. In addition, retail food prices for items not covered by the food import ban also increased 11.8 percent in 2014. Sugar and cereals prices rose by 40 percent and 34.6 percent respectively in 2014 while fruit and vegetables prices jumped by 22 percent.

**Figure 1. Russia: Price Increase of Selected Products (% y-o-y), 2014**



Source: PMR based on Rosstat data, 2015

From January-November 2015, inflation surpassed 12 percent. Prices for the following food products saw the highest increases in price rates from December 2014 - November 2015: sunflower oil 36 percent, fish and seafood 20.3 percent, pasta 18.9 percent, grain and pulse 15.3 percent, sugar 13.9 percent, bread and bakery 12.3 percent, milk and dairy products - 10.3 percent. The consumer spending landscape in Russia is characterized by regional disparities and consumers placing high priorities on essentials such as food, non-alcoholic beverages and housing. Approximately 29 percent of consumer expenditure in 2014 (31 percent in 2013) was allocated to the purchase of food and non-alcoholic beverages.

Russia's food processing industry had been growing steadily since 1998 with an annual increase of 15-25 percent. From 2005-2012, the compound annual growth rate of the industry (CAGR) totaled 16.5 percent. However, after the 2008 crisis, the sector growth rate slowed significantly. The food processing industry's production index in 2013 (0.6 percent) was almost as low as in crisis period in 2009 (0.3 percent) - however in 2014 it grew up to 2.5 percent. In 2014, market analysts reported that total food production reached 4.7 trillion rubles (\$123.4 billion) with 0.6 percent increase in number of businesses and 9.7 percent growth of food production value. The highest growth was reached in vegetable oil (21 percent), canned vegetables and mushroom preserves (17.6 percent); meat and offal (12.8 percent); butter (11.5 percent); meat and soya containing preserves (8.4 percent); pasta products (8.3 percent); poultry and offal (7.5 percent); semi-finished meat products (6.8 percent); cheese and cottage cheese (6.5 percent); mineral water (5.9 percent) and sugar (5.1 percent).

The food processing sector has garnered special attention by the Russian Government (GOR) supported

by import substitution policy defined as a national priority. Market analysts have stated that it could soon become one of the highest yielding sectors in Russian agriculture. The GOR defines the following targets for the industry: to improve the efficiency of enterprises, to provide diversification of production and to improve the competitiveness of manufactured products. In 2010, the GOR passed the “Principles of the Russian Federation State Policy in the Field of Nutrition until 2020” which is considered by many market players as progress in terms of GOR support for the food processing industry including food ingredients manufacturers.

The main objectives of the policy are: expansion of domestic production of basic raw materials that meet modern standards of quality and safety, the development of manufacturing food products enriched with essential components, specialized baby food, functional food products, dietary (curative and preventive) food products and dietary supplements. Also, the GOR pays attention to the development and implementation of innovative technologies in agriculture and the food industry, including biotechnology and nanotechnology, and development of healthy eating educational programs for various groups of the population. In this regard, technical regulations relating to food are expected to be adopted. Proposals to strengthen the legal responsibility of the manufacturer for production of food products which are consistent with statutory requirements, and to improve quality control mechanisms for food and raw materials produced in Russia and imported from abroad. Also, according to the document, the GOR would provide the conditions for investment in production of vitamins, enzymes for the food industry, probiotics and other food ingredients, consumer foods enriched with vitamins and minerals, as well as would prioritize development of research in the field of modern biotechnological and nanotechnological methods to obtain new sources of food and biomedical estimation of its quality and safety.

Along with the “Principles of the Russian Federation State Policy in the Field of Nutrition until 2020”, in order to develop an innovative environment for the food processing industry, the Ministry of Agriculture of has developed a "Strategy for the Development of the Food Processing Industry of the Russian Federation until 2020", which was approved by the Federal Government in April 2012. The strategy sets the following goals:

- increasing production volume;
- manufacture modernization and expanding capacity of food manufacturing enterprises;
- increasing products competitiveness with purpose of import substitution and export potential development;
- development of the food market infrastructure and logistics;
- addressing environmental concerns.

To reach such lofty goals, the GOR plans an influx of investment reaching 400-778 billion rubles (\$13-26 billion) which is deemed necessary to replace obsolete equipment, upgrade food processing technologies, introduce bio- and nanotechnologies, improve efficiencies in production facilities up to 85 percent, implement innovative engines and labor efficiency by applying IT and Enterprise Resource Planning (ERP) business management solutions. According to the 2013-2020 Development Strategy, the GOR expects to see the construction of 64 processing plants and renovation of 296 existing plants. However, these investments will need to be privately funded rather than through public funding.

The GOR also runs the industry-specific programs:

- “Development of Oil-and-Fat Industry in the Russian Federation for 2014-2016”
- “Development of Flour-and-Cereal Industry in the Russian Federation for 2014-2016”
- “Development of Beet-Sugar Sub-complex of Russia for 2013-2015”

According to the Program on oil-and-fat industry development, by 2016, production of vegetable oil will reach 4.5 million metric tons (MT), margarine – 480,000 MT, tallow drippings – 400,000 MT, spreads – 140,000 MT, mayonnaises, sauces in basis of vegetable oil – 860,000 MT, and oil meal – 5.1 million MT. The allocated budget for the program realization is 34.5 billion rubles. More details on the industry-specific programs are available at the [official site of the Ministry of Agriculture](#).

On December 29, 2014, President Putin signed Federal Law No.467-FZ, amending the Federal Law on Development of Agriculture (No.264-FZ of December 29, 2006). Such action extends the system of soft-term agricultural loans (partial compensation of interest rates) to organizations and individual entrepreneurs that process and market agricultural products. Processors of agricultural products also have access to the soft-term loans for owned or rented facilities. The loans are available to those whose income from processing/marketing of processed agricultural products is not less than 70 percent of their total income. The interest rate compensation component will be in effect until January 1, 2021. The federal funds for this compensation package are allocated from the federal budget through subsidies to provinces. The Federal Law No. 467-FZ of December 29, 2014 came into force on January 1, 2015.

The food processing industry is made up of foreign and domestic manufacturers with the latter dominating number wise. The biggest Russian food manufacturers are: Baltika Brewery Company, Cherkizovo Group of Companies, Efko Groups of Companies, Obyedinyonnye Konditery, Solnechnye Produkty, and the Ostankinskiy Meat Processing Plant. Among the most well-known foreign food manufacturers in Russia are PepsiCo Russia, Nestle Russia, Mars, Coca-Cola HBC Eurasia, Mondelez Rus’, Sun inBev, Danone Russia, McDonalds, Cargill, and Heineken United Breweries. These foreign investors are strengthening their positions with investments and marketing activities that overshadow domestic companies. Many Russian food processing companies are interested in forming strategic alliances with foreign partners. The main goals are access to technical knowledge, strengthening the company’s image in the market, access to cheaper financing, and personnel training. The leaders in this market are focused on consolidation and expansion into regions outside of Moscow and St. Petersburg.

After almost 18 years of negotiations, Russia acceded to the WTO on August 22, 2012 and became its 155 Member. The major WTO membership consequences for the food processing industry are a boost in strategic investors’ confidence, which could lead to technological innovations in the agricultural and food sectors in terms of the ability to produce healthy functional foodstuff, frozen fruit and vegetables and alcohol-free drinks. To get more information on the market access changes for each key food products that occurred with WTO accession for the U.S. suppliers please see the [GAIN Report](#).

**Table A. Russia: Food Processing Sector 2011-2014**

	2011	2012	2013	2014	2014/2013 (% change)

Number of businesses, including beverage and tobacco manufacturers (as of the beginning of the year)	40,869	41,274	43,016	43,263	0.6
Value of food production, in billion RUR	3,602	4,001	4,272	4,685	9.7
Value of food production, in billion USD*	122.73	128.77	131.36	123.37	-6
Production index, percentage change from previous year**	103.9	104.1	100.6	102.5	1.9
Balance, financial (profit less loss), in billion RUR	114.13	189.17	184.83	191.08	3.4
Balance, financial (profit less loss), in billion USD*	3.89	6.09	5.81	5.03	-13.4
Bread/bakery products, in thousand tons	6,626	6,507	6,711	6,537	-2.6
Flour, in mil tons	10	10.2	9.9	9.7	-2
Pasta products, in thousand tons	1,035	994	915	991	8.3
Confectionery, in thousand tons	3,037	3,107	3,288	3,423	4.1
Meat, incl. offal, in thousand tons	1,222	1,342	1,711	1,930	12.8
Poultry, incl. offal, in thousand tons	3,028	3,405	3,610	3,881	7.5
Sausages, in thousand tons	2,335	2,352	2,311	2,357	2
Semi-finished meat, in thousand tons	1,934	2,253	2,501	2,672	6.8
Fish and fish products, processed and canned, in thousand tons	3,642	3,689	3,788	3,644	-3.8
Milk, in thousand tons	4,926	5,267	5,386	5,317	-1.3
Butter, dairy spreads, in thousand tons	219	216	227	253	11.5
Cheese and cottage cheese, in thousand tons	1,127	1,180	1,167	1,243	6.5
Canned/preserved foods, in million cans (Standard can = 335 grams)					
• Vegetable and mushroom preserves	1152	1131	1247	1,464	17.6
• Fruit and vegetables juices, fruit nectars and drinks, juices for children	7978	8345	8175	8113	-0.8
• Dairy products	855	873	860	830	-3.5
• Meat and soya containing preserves	652	672.2	793	726	8.4
Vegetable oil, unrefined (including corn oil), in thousand tons	n/a	4,192	3,940	4,773	21
Sugar, beet and cane, in thousand tons	n/a	5,322	4,959	5,812	5.1
Water, mineral and carbonated, unsweetened and non-flavored, in million half-liters	n/a	10,578	11,080	11,732	5.9
Vodka, liquor products, in million deciliters	93.9	106.7	94.3	73.4	-22.2
Table wine, cava, in million deciliters	62.2	57.2	50.6	47.7	-5.7
Beer, in million deciliters	994	975	889	816	-8.2

\*The Dollar equivalent of “Value of Food Production” and “Balance, Financial” (i.e. net profit) is calculated based on annual average USD/RUR exchange rate: 2010 – 30.36, 2011 – 29.35, 2012 – 31.07, 2013 – 31.82, 2014 – 37.97.

\*\*The “Production Index” is a relative indicator characterizing changes in production output over comparable periods. The aggregate index of production characterizes integrated changes in production of all types of goods and products and reflects changes in value generated in the process of production as a result of quantitative changes of physical volume of production.

The factors that have restrained faster growth in the food-processing sector are as follows:

- Dependence on import raw materials and lack of consistently high quality raw materials;
- Ruble devaluation;
- High taxation;
  - Higher prices of raw materials;
  - Cost of public utilities;
- Significant debt load;
- Lack of experience of introducing innovative products;
  - Underdeveloped quality control and testing infrastructure;
    - Problems with recruiting qualified personnel;
  - Sales and distribution problems of manufactured products;
- Logistics problems and lack of developed distribution system;
- Lack of a developed regional infrastructure and logistical challenges as the obstacle for extension to remote territories like Volga, Ural, Siberia and Far East regions;
- Lack of financing in necessary volumes, terms and at affordable interest rates;
- Current food import ban.

### **Impact of Food Ban on Food Processing Sector**

As a result of the recent food import ban, Russian importers have had to find new sources for roughly 40 percent of its agricultural imports. In 2013, agricultural imports accounted for 10.4 percent of total imports (USD terms). According to Business Monitor International, the following categories are at the most risk as they were sourced mainly from banned countries: red meats, poultry, dairy, fruit and nuts, vegetables, fish and many others. For a full list of banned items in English please see this [GAIN Report](#). Later in June 2015, President Putin signed decree extending Russia’s food import ban until August 5, 2015 (please see the [GAIN Report](#) for more detailed information).

In 2014, Russia’s imports of foodstuff contracted by 8 percent to \$39.7 billion. In the second half of 2014, food imports plummeted by 14.2 percent in comparison with a slight decline of 1.2 percent during the first half of 2014. The biggest decline in agricultural imports that year was seen with wheat down 55.4 percent, vegetable oils down 51.4 percent, barley down 42.3 percent, and cocoa containing products down 27.5 percent. Raw and refined sugar topped the list of products that saw a surge in imports in 2014, up 257.3 percent and 25.6 percent respectively. A low sugar beet harvest was the main cause of the large import growth seen in 2014.

The food import ban was one of the main reasons for falling food imports in 2014 and 2015. However, 60 percent of the decrease was offset by a growth in domestic production, primarily of pork and poultry, and the remainder was mostly covered by imports from alternative countries. From September - December 2014, the former Soviet countries have boosted exports of meat to Russia by 21.4 percent, butter by 86.1 percent, citrus fruits by 25.4 percent, sausages and canned meat by 36.2 percent compared to the same period in 2013.

### ***Meat and Poultry***

The list of banned products includes most HS codes of beef, pork, poultry meat and by-products, and also salted, pickled, dried and smoked meat. Despite the steady growth in pork and poultry production, Russia remains strongly dependent on imports of meat, especially beef. In volume terms, meat imports have gradually decreased - in particular in 2013 – falling by 6.1 percent. Russia is less dependent on poultry imports as domestic production has increased substantially over the last decade. Russian consumers are responding to the current economic crisis by purchasing more poultry meat given its competitive price compared with other meat types. The United States was the main supplier of poultry meat to Russia accounting for 60 percent (or 267,000 MT) of all poultry imports in 2013. About 16 percent (72,000 MT) came from EU countries. In 2014, Russia significantly increased broiler imports from Belarus (up nearly 30 percent), Brazil (up almost 150 percent), Argentina (up nearly 165 percent), Turkey (which first appeared in 2014) and Serbia (up roughly 140 percent). Despite the increase in imports from these suppliers, total broiler imports were 17 percent lower, by volume, in 2014 than they were in 2013. The largest source of broiler meat exports to Russia between January and May 2015 were from Belarus (55,809 MT) and Brazil (24,379 MT). During this period Belarus and Brazil accounted for approximately 89 percent of all Russian broiler imports. Other notable suppliers of broiler meat to Russia in January-May of 2015 were Turkey (6,986 MT) and Argentina (2,088 MT). Despite the increase in imports from Belarus (+17.97 percent), Brazil (+54.6 percent) and Turkey (started poultry exports to Russia in August 2014) from January to May 2015, total broiler imports were approximately 50 percent lower than during the same period in 2014.

Meanwhile, the opportunities for non-restricted exporters will also be reduced in a market saturated with competitively priced domestic broiler meat supported by exchange rates favorable to local producers.

Several industry leaders in Russia have announced new investment projects which will expand broiler meat production in 2016 and beyond. For example, “Agrosila” (in Tatarstan), “GAP Recourse” (in Tambov Region), “Agrokomplex” (in Krasnodarskiy Krai), “Reftinskaya” (Sverdlovsk region), “Miratorg” (in Bryansk) and other producers have announced new projects involving either purchases of production plants and/or modernization projects. The Ministry of Agriculture has published a list of 65 projects totaling 64.9 billion rubles (over \$1.1 billion) investment in additional poultry production in 2015-2016. As these projects reach finalization, they will increase production capacity by 455,000 MT of poultry meat products. However, despite the increase in plant production and stabilization of feed costs, the market is still expected to experience slower growth in 2016 in comparison to the previous few years. The demand for poultry meat as a better priced alternative to red meats is likely to stabilize at 2015 levels. Meat processors are not expected to increase the share of poultry components in their products in 2016 as they did in 2014 and 2015. Russian government officials have reported that the purchasing power of Russian consumers is expected to stabilize in 2016 which may result in some consumer demand shifting back to pork. For more information on poultry production, please refer to GAIN report: [RS1554 Poultry and Products Annual](#).

Beef is the meat type which is most dependent on imports. In June 2015, the GOR extended a ban on a variety of agricultural products (including HS codes 0201, 0202, and 0210) from the United States, Canada, the European Union, Australia and Norway until at least August 6<sup>th</sup> 2016. In addition, the GOR issued a decree extending the ban to include Albania, Montenegro, Iceland, Liechtenstein, and Ukraine in August 2015. Russian beef imports have fallen by more than 30 percent between January 2014 and July 2015 due to a number of factors including trade interruptions, price volatility in the meat market, ruble depreciation and, finally, declining demand for beef in the stressed economy. Market analysts are reporting that domestic suppliers have enough capacity to meet only 60 percent of the existing demand.

Beef accounted for approximately 55 percent of all Russian meat imports in the first half of 2015 (compare to 32 percent for pork and 13 percent for broiler meat). Between January and May 2015, Russia imported 157,025 MT (PWE [1] ) of beef, mostly from Brazil (57,765 MT; 34.9 percent decline YTD [2] ), Belarus (52,137 MT ; 12.6 percent decline YTD); Paraguay (33,039 MT; 10.3 percent decline YTD) and Ukraine (8,265 MT 123% increase YTD) [3] . Brazil, Belarus and Paraguay jointly accounted for more than 90 percent of total beef shipments to Russia from January - May 2015. Brazil and Belarus will likely remain the biggest beef exporters to Russia in 2016 – particularly during the ongoing food import ban - with growing beef shipments coming from Belarus.

Domestic beef production has been declining in Russia over the last 25 years. Industry experts agree that major issue for Russia's beef production sector is limited access to affordable long-term credits. GOR officials have recognized that import substitution for beef will require a longer period of time and significantly higher investments to replicate the success of local pork and poultry producers and that self-sufficiency in beef and dairy can only take place after continued strong government support of the sector over the next decade. Contrary to the negative trend in the dairy sector, specialized beef-cattle projects are showing positive results and the use of beef cattle for beef production is expanding. According to Ministry of Agriculture officials, total investments of 10.2 billion rubles in 53 specialized beef projects will result in an additional 24,000 MT of beef production in 2015. ABH "Miratorg" is continuing the development of major beef cattle projects in Bryansk, Kaliningrad, Orel and Kaluga regions. Annual planned capacity of the new Miratorg processing plant in Bryansk is 130,000 MT of beef and beef products and the company expects to supply 40,000 MT of beef to the market by the end of 2015. "Zarechnoye" is planning to increase beef production in the Voronezh region by more than 10,000 MT (live weight) in 2015. Large-scale beef cattle projects are also being implemented in the Leningrad Region ("Sputnik"; "Losevo"), Krasnodarsky Krai (ZAO "Agrokomlex"); Orenburg Region ("Orenbeef" implemented as a pilot project of Italian "Cremonini Group") and in Kalmykia.

As noted above, pork (HS Codes 0203 and 0210) was included in the food import ban currently in place until August 2016. Additionally, pork trade is limited due numerous "sanitary restrictions" imposed by Rosselkhozadzor. As of August 1, 2015, roughly 25 percent of pork TRQs have been utilized. The Russian Federal Customs Service reported a reduction of more than 50 percent in pork imports from January – May 2015 compared to the same period in 2014. Only 4 countries have continued to ship pork to Russia, which are comparable or better in volumes than in previous years: Brazil (53,613 MT; - 5.26 % YTD), Ukraine (10,680 MT; +1665% YTD), Chile (4,690 MT; +7.97 % YTD) and Serbia (3,047 MT; +35.7 % YTD).

The Russian swine herd at large commercial plants has been growing over the last decade and the trend will most likely continue in 2016. The Ministry of Agriculture published a list of 79 projects with total

investment reaching 124.1 billion rubles for pork production. Several industry leaders including, but not limited to, ABH “Miratorg”, “Cherkizovo”, Group “Prodo”, “Omsky Bacon”, “Promagro” announced large expansion plans that are expected to increase pork production capacity by 330,000 MT (live weight) in 2016. The intensive growth of large-scale agricultural establishments will offset the significant decline in swine inventories of backyard and small private farms, which is primarily attributable to continued efforts to control African Swine Fever (ASF). According to Rosstat, the growth of the commercial swine herd has been registered in all federal districts with total swine inventories growing by 5.4 percent in the first half of 2015. Russian pork producers have benefited from the stabilization in feed prices and continued trade restrictions applied to many traditional exporters.

As a result, they have been able to increase the supply of domestically-produced meat to the market while increasing the swine herd. Russian pork production is increasing in many parts of the country with the fastest growth being reported in the Central Federal District. GOR officials have made many press statements highlighting continued support for large commercial producers that are capable to expand production due to operational experience, internal financial funds and highly qualified staff. The officials also noted that large operations apply better management practices mitigating the risks related to ASF. Industrial swine producers, represented by the National Union of Pork Producers (NUPP), expect to see further production consolidation in the future with up to 80 percent of all pork meat coming from the top 20 largest companies by 2020. NUPP also anticipates that up to 80 percent of all new facilities will be located in the European part of Russia - Central, Northwestern and Volga Federal Districts – as these are the most densely populated areas in the country.

The negative effects of trade interruptions and price volatility in the pork market are expected to recede somewhat in 2016 as domestic producers are slated to supply more reasonably priced pork to the market. Consumer demand is also expected to shift back to pork from poultry once the economy passes the peak of the current crisis.

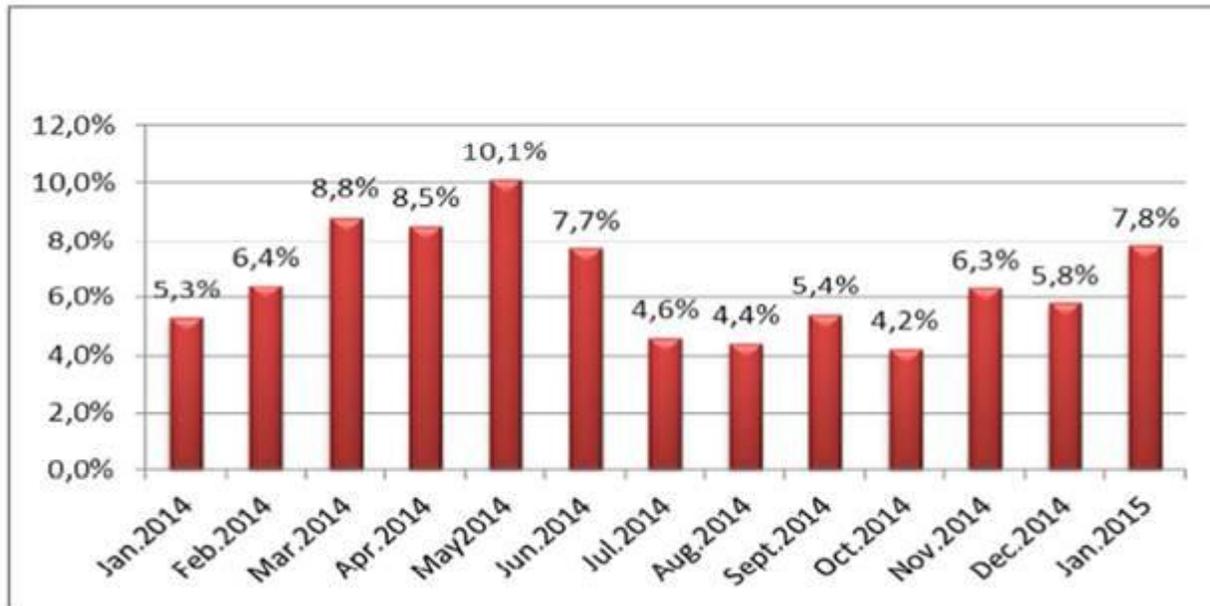
Russian Ministry of Agriculture officials have stated that the budget allocated for supporting agricultural producers in 2016 will remain at 237 billion rubles (3.95 billion USD), roughly the same as in 2015 ([RS1539 Agricultural budget 2015](#)). The main programs in the meat and livestock production sectors are anticipated to remain unchanged. However, the amounts distributed under each program may change. Currently, the most important financial support GOR provides to meat producers (poultry, pork and beef) is compensation of interest rates for long-term (investment) and short-term (operational) loans. Eligible beneficiaries receive subsidies from both federal and regional budgets. There is a requirement that only those companies participating in “matching” regional programs may apply for federal subsidies. In other words, regional governments have to allocate funds for “matching” federal programs. This form of support is currently taking place in 2015 but with some changes compared to previous years. For more details, please refer to [Livestock and Products Annual Report](#).

In 2015, the GOR introduced a new form of support for dairy and beef cattle projects - reimbursement of direct capital investments. According to Russian Ministry of Agriculture officials, 4 billion rubles will be directed for this purpose in the dairy sector in 2015, 7 billion rubles in 2016, and 8 billion rubles in 2017. The subsidies under this program will be paid directly to companies as soon as the construction or modernization of the production facilities is completed.

Russia’s meat-processing industry has evidenced a robust growth in recent months - up 6.9 percent in

Q4 2014 and 7.8 percent in January 2015. The food import ban contributed to the expansion of local production. In 2014, Russia produced 2 million MT of meat (up 13.3 percent), 3.4 million MT of poultry (up 7.8 percent), 2.4 million MT of sausages (up 1.9 percent).

**Figure 2. Russia: Monthly Growth Rates of Meat-Processing Industry, Jan 2014 - Jan 2015**



Source: Russian Federal Statistic Service, Interfax-CAN's analysis

Output of case ready meats and pork saw the fastest growth last year, up 14.4 percent and 13 percent respectively. Production of poultry and products outperformed the industry as well.

**Table B. Russia: Growth of Subindustries of Food Industry**

	Q3 2014	Q4 2014	000' tons	2014	Jan. 2015
Beef	-9.1%	-4.4%	175	-6.9%	0.8%
Pork	10.1%	17.6%	1 402	13.5%	24.8%
Poultry and products	9.3%	13.7%	3 881	7.8%	15.9%
Meat semi-products chilled	1.3%	0.1%	1 691	3.5%	-1.2%
Case ready meats chilled	16.3%	22.9%	53	14.4%	5.2%
Sausages	0.7%	-1.2%	2 539	1.9%	-1.0%
Canned meat, mln cans	2.9%	-1.3%	611	0.0%	14.6%

Source: Russian Federal Statistic Service, Interfax-CAN's analysis

### **Milk and Dairy Products**

The growth in production of processed dairy products in 2016 is anticipated at a slower pace than in

2014 and 2015, and Russian commercial dairies will most probably increase supply for factory use.

Belarus will remain the almost exclusive exporter of raw milk due to the current food import ban and weak ruble. Belarus accounted for 174,490 MT, valued at \$110 million, or 97.5 percent of Russian imports of fluid milk from January to July 2015, which is an approximately 1 percent decline in volume and a 30 percent decline in value compared to the same months of 2014. The total volume of fluid milk imports to Russia was 22.5 percent lower than in the same months of 2014. The total value of milk imports declined 53.72 percent. The average price per one MT of fluid milk dropped from \$1,105.66 in July 2014 to \$631.26 in July 2015. This decline in prices is a result of factors including lower demand for imported milk from Russian dairy processors, the depreciation of the ruble, and low world commodity prices for milk. Russia remains the major market for milk and dairy from Belarus as 98.65 percent of dairy exports from Belarus go to the Russian market.

Russian officials have stated that the budget for supporting agricultural producers in 2016 will remain at 237 billion rubles (\$3.95 billion), the same as in 2015 ([RS1539 Agricultural Budget 2015](#)), hence the current programs of dairy sector support will most likely continue in 2016 at the same level in order to meet import substitution goals for dairy. The Ministry of Agriculture published a list of 166 new dairy projects with a planned 24.3 billion rubles (approximately \$367 million) in total investment. The successful execution of the projects, all of which will be receiving subsidies from the federal and regional budgets, could further offset the continued decline of production at household farms in the coming years. According to Rosstat, during the first half of 2015, agricultural establishments increased milk production by 2.4 percent (250,000 MT), small private farms also increased production by 5 percent (45,000 MT), household farms decreased output by 3.6 percent (250,000 MT). The share of commercial dairies in total milk production is gradually growing, and the trend is anticipated to continue in 2016.

According to industry analysts, limited access to affordable long-term credit constrains modernization and growth of commercial milk production. The level of consolidation in milk production sector is low.

According to Ministry of Agriculture, the top ten companies produced only 536,000 MT of milk in 2014, which is approximately 3 percent of all the raw milk processed at dairy plants in Russia. Smaller dairies experience difficulties in obtaining credit for operational costs and further development. Business is addressing the issue by joint projects between milk producers and milk processors. Leading processing companies launched projects in 2015, such as advance payments for milk to be delivered in two years, to assist local milk producers, which will contribute to improved production in the next few years.

The Food Security Doctrine adopted by the GOR in 2010 defined the self-sufficiency goals for the dairy product group at 90 percent, but in 2013 imported products accounted for 40 percent of total cheese consumption. Since the GOR put in place the counter-sanctions embargo in August 2014 and with renewed focus on import substitution policies, cheese imports dropped to under 20 percent of consumption in 2015. According to official Rosstat data production of cheese and cheese products grew by 25 percent and curd production increased by 9.6 percent in January-August 2015. In 2013 Russia imported approximately 465,000 MT of cheese and curd, of which more than 56 percent (261,500 MT) were quality products from the EU. Imports accounted for approximately 40 percent of cheese consumption in Russia in 2013. In August 2014 the GOR banned several traditional western suppliers, causing cheese imports to drop 25 percent in volume in 2014 compared to 2013. A second shock for the cheese market came from steep ruble depreciation and accelerated inflation in 2014-15, which made

imported products much more expensive. As a result of the food import ban and recession, total imports of cheese and curd dropped in volume by 51 percent from January-July 2015, while the value of these imports fell by 65 percent compared to the same months of 2014.

Domestic cheese producers responded to the reduced supply and have been increasing production since August 2014. The sharp increase in demand for quality milk from cheese makers inflated the commodity price for raw milk in the end of 2014. Some cheese producers in response to increased raw milk prices switched from production of dairy cheese to production of lower priced cheese products with non-dairy fat substitutes. The average price for domestically produced cheeses grew between August 2014 and February 2015, then dropped as Russian consumers switched to lower quality, less expensive foods due to falling disposable income. Russian authorities and producers of quality dairy cheese are concerned about widespread improper labeling of cheese products with non-dairy components.

According to recent expert estimates, the share of cheese products with non-dairy fat substitutes labeled “dairy cheese” may be between 10 and 30 percent. As a result of these events in 2014-2015, consumers partially replaced quality dairy cheeses they were buying in 2013 with cheese products containing non-dairy fat substitutes, which in some cases are labeled “dairy cheese”. The GOR and dairy industry are concerned about the issue of increased use of non-dairy ingredients in dairy products. Professional associations and Ministry of Agriculture officials and legislators in the State Duma addressed the issue and proposed several initiatives such as limiting palm oil imports, making changes to the EAEU technical regulations in terms of labeling requirements for milk-containing products, introducing bigger fines for violation of dairy products labeling regulations, etc.

As a result, the GOR has launched the process of amending the Customs Union Technical Regulations on Safety of Milk and Dairy Products. However, industry experts expect the use of non-dairy fat substitutes to decrease only after a recovery of consumer demand for quality cheeses and stabilization of cheese prices. Food processors are also skeptical about any limitation of palm oil imports because it is also used in confectionary and bakery products. According to various estimates, dairy processors may utilize approximately 25-30 percent of the imported palm oil. The recent food import ban has not spread to the key categories of high-tech food ingredients, the alternatives for which are difficult to find in the domestic market. The replacement of rennet cheeses which is not available at the moment from the EU can be rennet casein: it can completely replace rennet cheese or cottage cheese in the production of all types of processed cheese. Another option of high demand among cheese manufacturers is the use of milk protein concentrate. Given the shortage of raw milk, MPC (milk protein concentrate) is becoming increasingly popular.

Domestic butter producers were able to maintain production growth in 2015 and partially replace missing imports, although at a slower pace compared to the previous year, when annual production volume increased by 15 percent. According to official statistics, 2015 butter production was 6.2 percent higher in January-August than in the same period in 2014. Domestic producers benefit from the reduced competition in the market due to current trade restrictions for some western suppliers.

Meanwhile, similar to cheeses, the use of non-dairy fat substitutes in butter has reportedly increased since August 2014. Trade interruptions in 2014 – 2015 and current economic difficulties had a minor impact on volume of butter consumption in Russia, as local producers and exporters from Belarus were able to increase production and supply enough butter to the market. Retail prices for butter increased by

10 percent between November 2014 and March 2015 from 352.18 rubles per Kg to 388.76 rubles following a sharp ruble depreciation. However, unlike cheese prices, retail prices for butter remained stable between March and September (386.07 rubles per Kg) 2015 reflecting balanced supply and demand of the product in the current market. Dairy butter is included in the food import ban currently in place until August 2016. As a result, the number of countries exporting butter to Russia has dropped. From January-July 2015 only 8 countries shipped butter to Russia: Belarus (39,695 MT; increased exports in volume by 51.91 percent), Uruguay (4,725 MT; decreased by 25.9 percent), Argentina (2,318 MT, 61.18 percent decrease), New Zealand (2,063 MT. 84.75 percent decrease), Brazil, Kazakhstan and Moldova shipped less than 500 MT combined. Belarus accounts for 81 percent of Russian butter imports in 2015, and is expected to remain the biggest supplier in 2016. Some growth of butter exports from New Zealand may be seen in 2016.

According to Rosstat, production of Whole Milk Powder (WMP) declined by 13 percent in January-August 2015 compared to the same period in 2014. This decline mostly reflects the decline in demand for WMP from processed food producers. Shipments from Belarus may take a greater share of consumption because Russian WMP producers compete with Belarusian supplies, who benefit from stronger state support and lower commodity milk prices. Food producers in Russia reportedly prefer imported WMP to domestic due to the lower quality of local WMP. Rosstat also reported a decline in Non-Fat Dry Milk (NFDM) production by 16 percent in January-August 2015 (by approximately 12,000 MT). At the same time, according to Federal Customs Service, imports of NFDM increased 22 percent (by approximately 10,000 MT) in January-July 2015. Total supply of NFDM in January-July 2015 remained at 2014 levels, indicating stable demand for milk proteins in the market. NFDM production in 2015 is forecast at 70,000 MT, this is a 16 percent (14,000 MT) decrease in output compared to 2014 [1] .

Production of milk powders in Russia tends to grow in the 2<sup>nd</sup> and 3<sup>rd</sup> quarters of the calendar year, which reflects the seasonality of fluid milk production in the country. Dairy processors can't use all raw milk during "high milk season" partially because consumer demand for dairy falls from May to September. Processors usually increase the use of powders during the fourth and first quarters of the year, when commodity prices for raw milk are high. NFDM is widely used in dairy products sector for low fat traditional products (tvorog, kefir) and cheese products with non-dairy fat substitutes. WMP is used by confectionary, bakery and processed meat food producers. The Food Embargo [Report](#) published by The Analytical Center of the Government of Russian Federation in August 2015 noted that trade restrictions imposed on several western suppliers resulted in "reduced diversification of supply channels for milk powders to Russia". Thus, according to the Federal Customs Service of Russia, in 2014 the country imported NFDM from 24 different countries and WMP from 14, compare to only 6 countries shipping dry milk powders to Russia in January-June 2015: Belarus, Argentina, Switzerland, Uruguay, Kazakhstan and Armenia. Belarus, which accounted for 76 percent of NFDM and 80 percent of WMP imports to Russia in Jan-July 2014 increased its share to 95.42 percent for WMP and 95.95 percent for NFDM in the first half of 2015.

Multiple research polls conducted by official and private organizations indicate that Russian consumers switched to less expensive foods in 2015. For example, the GFK report shows growth in volume in the following dairy categories: fluid milk by 3 percent, kefir by 1 percent, sour cream by 6.2 percent, curd (tvorog) by 3.5 percent, and processed cheese products by 14.9 percent. At the same time sales (in volume) decreased in more expensive groups: hard cheese declined by 6.8 percent, and drinkable

yogurts by 3.6 percent.

For more information, please refer to the [Dairy and Products Annual Report](#).

### **Confectionary**

The current economic crisis certainly affects the development of the confectionary sector. First, the industry has demonstrated a shift in demand to cheaper segments, which was to be expected. Many market analysts predict a continuing rise in popularity of inexpensive analogues of premium products and so-called “fast sweets” such as chocolate bars, which can be a quick snack under time pressure.

Export-oriented confectionery production is expected to become more promising. Domestic manufacturers dominate the Russian confectionery market whose share account for around 88 percent. Though “domestic manufacturer” is a bit misleading since many international companies have set up the manufacturing in the country. During the last five years, domestic production has been increasing. The 2013 production increase made possible the ability to see export growth for flour confectioner’s goods by 22 percent and for sugar confectioners’ goods by 16 percent. In 2014, the total output of confectionary products increased by 4.1 percent.

**Table C. Russia: Output of Confectionary Products, in Thousand MT**

<b>Year</b>	<b>2010</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2013/2014 % change</b>
Flour confectionary, tarts and cakes, short-life	329	341	343	367	6.9%
Biscuits, honey gingerbreads, wafers	1,097	1,186	1,210	1,291	6.7%
Cacao, chocolate, sugar confectionary	1,464	1,581	1,735	1,765	1.7%

*Source: Rosstat, Federal Customs Service*

The highest profit ratio among the biggest chocolate manufacturers is demonstrated by “Konditerskiy Concern “Babayevskiy” (17.9 percent), “Mars” (15.5 percent) and “Ferrero Russia” (15.3 percent), according to the highly respected agency “Kredinform”. The value share of “Ferrero Russia” is 15 percent in the segments where its products are presented including packed chocolate, biscuits, chilled snacks, chocolate spread and cooling candies. “Nestle Russia” is the second biggest food processing company in terms of sales volume but it has a relatively low return on sales (4.8 percent) which is explained by the diversified nature of its business: the enterprise manufactures not only chocolate but also coffee, breakfast cereal, baby food, tarts, pet food and other products.

According to Rosstat, the share of import chocolate totaled 15 percent of the Russian chocolate market during recent years. In 2015, imports of chocolate products decreased by 50 percent due to the ruble depreciation and weaker consumer demand. In January-July 2015, chocolate and sugar confectionary imports totaled around 52,000 MT which is almost twice less than in the same period of 2014.

However, domestic chocolate producers have not been able to fully substitute the amount of dropped volumes. Though the share of imported chocolate in retail decreased from January-August 2015 while domestic chocolate production decreased by 1.4 percent compared to the same period of 2014 and totaled 1 million MT. As for the segment of packed chocolate and cocoa containing products, the production from January – June 2015 decreased by 18.4 percent compared to the same period in 2014

and totaled 44,400 MT. Output of sweets containing alcohol dropped by 29.4 percent (14,700 MT). Production of cocoa powder without adding sugar and other sweeteners decreased by 13.6 percent (2,200 MT), cocoa powder with sugar – down 26.6 percent to 3,900 MT.

Industry analysts explain the problem of chocolate import substitution by the fact that domestic chocolate and imported products occupied different price niches: more than 50 percent of imported chocolate and sugar confectionary had occupied the premium segment during the last decade while domestic manufacturers traditionally occupied the mass segment of the market. A falling ruble, weak consumer demand, and growth of operating costs have all contributed to manufacturers’ product-line expansion in the direction of the above-average or the premium segments. Import substitution in the production of chocolates and sugar confectionary could be supported by a reduction in fiscal and administrative barriers.

Another serious problem for domestic chocolate manufacturers is restricted import of key ingredients. Chocolate production in Russia is very dependent (roughly 60 percent) dependent on imported ingredients. Due to the ruble depreciation, the cost of cocoa-products used for manufacturing chocolate has increased by more than 50 percent compared to a year earlier. The cost price ratio was also influenced by the food import ban which restricted supplies of nuts and dried fruits from EU, U.S., Canada, Australia and Norway. In November 2014 Russian company “Babayevskiy came close to stopping production of some confectionary products due to food import ban. Later in early 2015 “Krasnyi Oktyabr” and “Babayevskiy” advised that prices would increase because of the growing costs of imported ingredients. Moreover, the costs for sugar and dairy products have also grown while these ingredients have between 14-25 percent share in the cost price structure of chocolate manufacturing. The retail price for 100 grams of chocolate in Russia grew by 38 percent within one year: from 49.1 rubles in March 2014 to 62.1 rub in March 2015. It is important to note that manufacturers cannot increase their prices in proportion to the growth in their expenses.

### ***Micro-Ingredients and Additives***

Micro-ingredients and additives are largely imported to Russia. According to the RBC research, the Russian market accounts for roughly 10 percent of the \$28.3 billion world market of food ingredients estimated to be worth around \$2.8 billion in 2013. Market analysts characterize the ingredients and additives market in Russia as developing and non-saturated with good room for growth.

**Table D. Russia: Food Ingredients Market’s Consumption and Rate of Growth, 2006-2015**

<b>Year</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>
Consumption (\$ billion)	1.7	2.0	2.3	2.0	2.1	2.3	2.6	3.0	3.4	3.9
Rate of growth, %	n/a	15%	15%	10%	5%	10%	10%	15%	15%	15%

*Source: Union of Food Ingredients of Russia*

According to the Russian Union of Food Ingredients, at present the Russian food processing industry uses more than 20 types and about 1,000 varieties of food ingredients and additives such as acidity regulators, sweeteners, bleachers, colorants, emulsifiers, thickeners, preservatives, nutrition fortifiers, flavors, pectins, starches, fats, stabilizers, and so on. *RBC Research* analysts inform that the market

volume of Russia's food micro-ingredients totaled \$3 billion in 2013 and showed 7 percent annual growth. Russia's food ingredients market is weighted as follows: flavors (29 percent), preservatives (24 percent), colorings (19 percent), antioxidants (13 percent), food acids (6 percent), and cloud emulsions (2 percent). The main consumers of ingredients are bakery, confectionery, dairy (including ice cream manufacturing), meat processors and canned and bottled food producers.

The major players in the global market of micro-ingredients includes ABF Ingredients, Kerry Ingredients & Flavors, Cargill Food Ingredients, IFF, DuPont, Givaudan, Firmenich, Symrise all of which are represented in Russia by selling their own products through distributors. Several global manufacturers have opened their own production facilities in Russia as well. For example, Cargill launched its own plant in Efremov, Tula region. In 2010, Symrise (manufacturer of flavors) opened a plant in Podolsk, Moscow region. The plant can produce up to 9,000 MT of dry flavors for chips, crackers and instant food.

In contrast to the global market, the Russian market is not concentrated. Competition in the Russian market of food micro-ingredients takes place between foreign and domestic manufacturers. And, according to market participants, this competition is getting stronger year by year. *RBC Research* estimates that the top 10 players in the Russian market of food micro-ingredients cover about 40 percent of the market (in terms of revenue). Moreover, almost a quarter is accounted for by Cargill (23.8 percent). Russian production of food micro-ingredients is strongly dependent on foreign supplies of raw materials. The largest Russian food micro-ingredients manufacturers prefer to work with the world's leading suppliers of raw materials and carry out strict selection. This approach is common mainly for major Russian players which have been operating in the domestic market for a long time and pay increased attention to product quality such as "PTI" group of Companies, "Valetok Prodimpeks", etc. The necessary condition for sales is strict quality control at the stage of procurement of raw materials, the reputation and reliability of the supplier. This approach significantly reduces the risks to produce products of better quality and to optimize the production cycle.

The trends of micro-ingredients world market are reflected in Russia. Growth in the Russian market is averaging 10-15 percent per year - significantly higher than in most countries. The majority of flavors is consumed by the Russian food industry is for production of alcoholic and non-alcoholic beverages (36 and 34 percent respectively. Intensive development is being seen in the food colorants industry. Market players forecast global growth to reach \$5.4 billion by the end of 2016 and up to \$20 billion by the end of 2020. The main consumers of this product are producers of non-alcoholic beverages (54.6 percent). The share of Russian market of food colorants is 1.5-2 percent of the world market. As well as the market of food flavorings, the colorants market is dependent on imports for almost 100 percent (both in terms of the finished product and from the point of view of raw materials). Natural colorants make up the highest part of Russian imports (85 percent in volume and 80 percent in value terms). The only manufacturer of a full cycle in Russian market is Chemical and Food Aromatics Plant (St. Petersburg), which produces natural food colorants using its own raw materials. The largest suppliers of domestic food colorants in Russian are Ecoresource, Bioline and others. Russian market of sweeteners is strongly represented by domestic producers of table sweeteners and mixed sweeteners for industrial purpose. "Marbiopharm" produces food sorbitol using its own raw materials. Russian companies are now actively engaged in development and production of mixed sweeteners. The major players in the domestic market are WorldMarket, "Arkomp" Group of Companies, "Zelyonyi List", "Aspasvit", "NovaProdukt AG", "Zelyonye Linii."

The growth of healthy food consumption is a world trend which also actively developing in Russia. The use of sugar substitutes and sweeteners is one of the major methods of creating food products with low sugar content. Following a global trend, Russian food processors more and more use sugar substitutes and intensive sweeteners most of which are imported from abroad. The key player in the market of glucose syrups is Cargill which controls more than a half market with the syrups manufactured at its plant in Efremov.

Antioxidants are widely used in the production of oil, flour confectionery, dairy products, meat, sausages, frozen foods, fish products, food concentrates, dry soups and broths, cereals, potato chips, etc. The EU is a major supplier of antioxidants to Russia, but lately many of these products have been coming from China. The segment of preservatives has a similar situation: almost all the preservatives used in Russian food industry are imported from China. Russian production of food preservatives is represented by manufacturing acetic acid, sodium nitrite and sodium pyrosulfite.

The trends in most segments of the Russian market of food micro-ingredients show strong dependence on imports. The share of imported ingredients and additives is roughly 85 percent compared to 15 percent being domestically produced. Around 90 percent of raw materials for micro-ingredients production are supplied to Russia from abroad as well as are most food additives and ingredients which are used by Russian companies. Based on the same source, China is the larger supplier of ingredients to Russia with 15.4 percent of total market share. Lithuania holds 12.5 percent of the market, Germany - 11.2 percent, the Netherlands - 9.7 percent. The United States exports some ingredients to Russia and ranks as the 11th biggest supplier with market share of 3.1 percent. Market analysts characterize the ingredients and additives market in Russia as “developing” and “unsaturated” with good room for growth in upcoming years.

However, Russia is very competitive market and China has been a constant supplier of less expensive products. European companies have invest a lot in education and training programs for the food processing companies and help their importers to build/strengthen demand for their products in Russia. Also, the Dollar/Euro strengthened against the ruble in 2014 making U.S. and European products much more expensive for Russia’s food processing sector.

**Table E. Russia: Imports of Micro-Ingredients in 2013-2014, in Thousand MT**

<b>Product</b>	<b>2013</b>	<b>2014</b>
Food Acids:		
<b>Citric Acid</b>	<b>19.1</b>	<b>21.35</b>
Dihydroxysuccinic Acid	<b>3.38</b>	<b>3.12</b>
<b>Lactic Acids</b>	<b>7.2</b>	<b>5.04</b>
<b>Gluconic Acid</b>	<b>1.62</b>	<b>1.69</b>
Sweeteners:		
Sorbitol	<b>30.7</b>	<b>25.6</b>
Mannitol	<b>1.01</b>	<b>0.8</b>
Saccharin	<b>0.25</b>	<b>0.26</b>
Preservatives:		

Acetic Acid	<b>17.8</b>	<b>1.7</b>
Benzoic Acid	<b>8.1</b>	<b>7.3</b>
Formic Acid	<b>6.4</b>	<b>5.2</b>
Propionic Acid	<b>0.91</b>	<b>0.98</b>
<b>Thickeners and Gelling Agents:</b>		
Pectin	<b>2.57</b>	<b>3.11</b>
Agar-agar	<b>0.27</b>	<b>0.437</b>
Locust Tree and Cluster Bean Gum	<b>5.6</b>	<b>5.6</b>
<b>Other Vegetable Thickeners</b>	<b>2.8</b>	<b>3.1</b>
Gelatin,	<b>6.7</b>	<b>5.7</b>
Modified Starches	<b>67.1</b>	-
<b>Water-retaining Food Additives:</b>		
Glycerin	<b>104.7</b>	<b>106.4</b>
Propylene Glycol	<b>24.9</b>	<b>21.3</b>
Lecithin	<b>4.2</b>	<b>5.5</b>
Glutamic Acid and its Salts	<b>9.2</b>	<b>8.75</b>
Vanillin	<b>0.325</b>	<b>0.352</b>
<b>Ethyl Vanillin</b>	<b>0.051</b>	<b>0.058</b>

*Source: All-Russian Research Institute of Food Additives*

A result of the food import ban introduced by the GOR in August 2014, Russian food processors have been forced to switch to alternative foreign and domestic suppliers of raw materials which resulted in lower quality, additional expenses and increased end-user prices. The weak ruble makes raw materials and ingredients much more expensive which has led to lower consumer demand and falling sales. Due to enormous efforts by the food ingredients business community, food manufacturers and industry associations, Government Resolution #830 “On Amending Resolution of the Government of the Russian Federation dated August 7, 2014, #778” dated August 20, 2014, excluded dietary supplements, vitamins and minerals, flavors, protein concentrates and mixtures (animal and plant) dietary fiber and nutritional supplements from the list of banned agricultural products, raw materials and foodstuffs originating from the United States, European Union, Canada, Australia and Norway.

The food import ban and ruble depreciation highlighted the country’s import dependence in the market leading GOR officials to announced support for developing domestic production of micro-ingredients and additives.

Domestic production of micro-ingredients will be supported by a special federal program until 2025, the project of which is under development. The program targets:

- providing Russian food processing industry with domestic micro-ingredients equal to foreign analogues in safety, quality and economical performances;
- decreasing Russia’s dependence on import of micro-ingredients for food industry and increasing food safety of the country;
- increasing safety and quality of food products using domestic micro-ingredients and avoiding foreign counterfeit.

The results of the program will correlate with “The Strategy of Food Processing Industry of Russian Federation until 2020” and “State Program for Development of Agriculture in 2013-2020”.

The Russian market is growing rapidly in the context of the world market trends:

- Moving away from artificial additives in favor of natural ingredients;
- The trend of environmental sustainability;
- The growing popularity of low-calorie foods sector;
- Market growth of functional ingredients;
- Development of new food technologies in the field of food ingredients.

The growth of consumer interest in high-quality, natural and environment friendly ingredients is leading Russian manufacturers to gradually switch to using organic raw materials and more “natural” ingredients in the Russian market.

## **Regulatory Framework**

Russia operates a complex and often unpredictable system of import controls, including sanitary regulations, import tariffs, import quotas and other restrictions. Barriers to trade have traditionally depended on the type of product, customs clearance location, importer status and other sometimes non-transparent factors.

Many of Russia’s food and trade regulations have or are undergoing reform as Russia continues policy integration with Armenia, Belarus, Kyrgyzstan and Kazakhstan via the Eurasian Economic Union, which replaced the Customs Union on January 1, 2015. For additional details, please see GAIN report [RS1478 Eurasian Integration Continues with the Eurasian Economic Union](#).

Below is the list of Technical Regulations governing the import of foodstuffs along with Russian Federal Laws, Russian Government documents, and regulatory documents of the bodies of executive power of the Russian Federation:

<<http://www.eurasiancommission.org/ru/act/texnreg/deptexreg/tr/Pages/default.aspx>>

- CU Commission Decision No. 319 of June 18, 2010 “On Technical Regulation in the Customs Union” (as amended through April 9, 2013)
- CU Commission Decision No. 526 of January 28, 2011 “Common List of Products which shall be Subject to Mandatory Requirements within the Customs Union” (as amended through November 23, 2012)
- CU Commission Decision No. 620 of April 7, 2011 “Common List of Products, Subject to Mandatory Evaluation (Confirmation) of Compliance within the Customs Union with the Issuance of Common Documents” (as amended through December 2, 2014)
- CU Commission Decision No. 621 of April 7, 2011 “On the Regulation on Application of Standard Schemes for Evaluation (Confirmation) of Compliance with Technical Regulations of the Customs Union”
- CU Commission Decision No. 711 of July 15, 2011 “On the Common Sign of Circulation of

Products on the Market of the Member States of the Customs Union (as amended through July 20, 2012)

<<http://www.eurasiancommission.org/ru/act/tehnreg/deptexreg/normbaza/Pages/EAC.aspx>>

- EEC Collegium Decision No. 293 of December 25, 2012 “On the Unified Forms of a Certificate of Conformity and a Declaration of Conformity with the Technical Regulations of the Customs Union and the Rules of their Execution”  
<<http://www.eurasiancommission.org/docs/Download.aspx?IsDlg=0&ID=3814&print=1>>
- CU Technical Regulation TR TS 005/2011 “On Safety of Packaging” (as amended through June 10, 2014)  
<<http://www.eurasiancommission.org/ru/act/tehnreg/deptexreg/tr/Pages/bezopypakovki.aspx>>

Controls and regulations on food additives are included in [SanPiN 2.3.2.1078-01](#) (Section 9) and [SanPiN-2.3.2.1293-03](#), “Hygienic Requirements for Food Additives.” These rules establish safety requirements for food additives in order to make products safe for human consumption. The total list of allowed food additives consists of several hundred items and is given in Attachments 1, 3, 4, 5, and 6 to the [SanPiN 2.3.2.1293-03](#). Rospotrebnadzor may prohibit or allow food additives based on safety tests.

In July 2012, the EEC adopted the Technical Regulation of the Customs Union on “Safety Requirements for Food Additives, Flavorings, and Technological Aids” (TR TS 029/2012), which contains a list of food additives allowed for use in food product manufacturing. The TR TS 029/2012 came into effect on July 1, 2013, and became the primary document regulating production and quality of products in the sector of food ingredients and additives. Production and circulation of products meeting the pre-existing CU and national requirements of the EAEU Member States was allowed during a transition period, which expired on February 15, 2015. For more information please see GAIN report [RS1338 Customs Union Technical Regulation on Food Additives](#).

Russia also continues to adjust policies pursuant to its World Trade Organization (WTO) accession on August 22, 2012. Russia and the Eurasian Economic Union (EAEU) have established the legal framework necessary for Russia to comply fully with the WTO Sanitary and Phytosanitary (SPS) Agreement. In addition, Russia undertook commitments on how it will comply with the SPS Agreement and its other WTO commitments affecting trade in agricultural products. These commitments provide U.S. exporters of agricultural products with an enforceable set of disciplines against non-scientific trade restrictions. Russia also agreed to harmonize Russia’s SPS measures with international standards. The Eurasian Economic Union has a mechanism for recognizing the equivalence of food safety systems of WTO members and rules on inspection of establishments in third-countries, such as the United States, that export product to Russia and the other EAEU Member States. Russia’s commitments also include, in part: increased transparency, including the right to provide comments on SPS measures before they are adopted, and application of transition periods before new measures are applied.

FAS Moscow’s Food and Agricultural Import Regulations and Standards reports identify major pieces of legislation that govern food, plant, and animal health, most of which received thorough review during the past few years’ WTO accession negotiations: [RS15100 Food and Agricultural Import Regulations and Standards - Narrative](#).

## **Advantages and Challenges for U.S. Exporters**

Companies from all over the world are looking at the Russian market to try and take advantage of improved market and/or regulatory access given Russia's recent WTO accession. Successful imports tend to be those that add to the variety of foods available on the market and products that are not grown in Russia or for which domestic production is insufficient to meet domestic demand. Food ingredients exporters should review some of the advantages and challenges of the Russian retail market when considering their marketing strategy.

**Table F. Russia: Advantages and Challenges for U.S. Exporters**

Advantages	Challenges
Population of 143 million people who are potential consumers.	Economic and political vulnerability, dependence on oil and mineral extraction for economic growth.
Russian food processing ingredients market is widening its assortment.	Increased Dollar rate made prices for imported raw materials and food processing ingredients from U.S. less affordable for manufacturers.
Demand for food processing ingredients is growing dramatically compared to the other sectors of the food processing industry.	Decreased purchasing power and per capita spending among the middle class, particularly in the regions, and the consequent lower demand for expensive food products.
Russian food processing sector mostly relies on imports.	Consumers are switching from imported products to cheaper brands or Russian analogs due to Ruble devaluation.
Share of imported ingredients is 86-90% against 10-14% of locally produced.	Growing number of domestically produced generic products; lack of knowledge of American products.
Russia is still an attractive market for a number of U.S. products including sauces, micro-ingredients, additives spices, pastas, beverage, etc.	Rapid development of local manufacturers of ready-to-cook products and Government Strategy to modernize food processing sector creates tough competition for similar imported goods.
Local processors more and more must meet international quality standards. They pay more attention to the quality of the ingredients they use and local ingredients often do not meet their needs.	Russian processors lack well-developed contacts with U.S. suppliers.
Russian food processing companies continue to expand and modernize their production facilities. This increases their demand for high quality ingredients.	Russian producers of ingredients are improving the quality of their products.
GOR's strategy for food processing industry development ensures increasing production volume, upgrading manufacturing facilities, expanding capacity of food manufacturing enterprises, and increasing products	Sales increase of locally produced ingredients is influenced by proximity to end-users, awareness of consumer demand specifics, operative decision of enterprises' technological problems, well-functioning logistics services, lower prices

competitiveness.	compared to imported products.
GOR has committed to spending billions on infrastructure over the next 10 years, particularly railroads and highways, which should translate to better logistics.	Imperfection of tariff legislation and its constant changes sometimes lead to customs clearance delays, contract disputes, and unpredictable expenses.
Urban life style increases demand for semi-finished and ready-to-cook products.	High credit rates create obstacles for inflow of foreign investment into Russian industry.
Growing demand for healthy food leads to increasing consumer demands for better quality and innovative/functional products, forcing processors to use high quality ingredients.	Cash-in-advance system of payment is still a common trade practice in Russia, due to credit risks and expenses from letter of credit.
Russia's retail sector is growing.	European exporters have geographical advantage, and exporters from the Middle East and China offer lower prices.
Due to the accession to the WTO Russia is obligated to bind its agricultural tariffs, adding more predictability to the trading relationship and opening export opportunities for the U.S. agricultural industry.	Russian government bureaucracy and grey market. Contradictory and overlapping regulations. Official government opposition to growth in food imports. Import substitution policy.
Significant number of consumers can afford purchasing high-quality food products.	Competition with food products imported from the EU and other countries may rise.
Existence of large importers experienced in importing food products to Russia.	Food sanctions' negative effect on trade. Competition with food products imported from countries which are not in the banned list has risen.

## SECTION II. ROAD MAP FOR MARKET ENTRY

### A. ENTRY STRATEGY

Of course, the best entry strategy for every new-to-market exporter depends on its unique experience, particular circumstances, and specific products. But there are some general recommendations for successful entry into the Russian market.

In order to make Russian processors aware of the assortment and quality of U.S. ingredients, plan to attend specialized exhibitions. There are three major shows held in Moscow that can be recommended for participation.

#### **World Food Moscow**

Moscow, ExpoCenter

September 12-15, 2016

<http://www.world-food.ru/en-GB/about.aspx>

World Food Moscow is a USDA-supported show, and is essentially the “main event” for U.S. exporters interested in market opportunities in Russia. ATO Moscow and the Office of Trade Programs (in Washington) organize American pavilions in the grocery, fruit, and seafood sections offering “turn-key”

service. USDA industry organizations (aka Cooperators) typically organize a pavilion in the meat hall. In 2014, this 4-day show drew more than 1,600 exhibitors from 72 countries and attracted more than 30,000 importers, wholesalers, retailers, and processors from all parts of Russia and from many neighboring countries.

### **Prodexpo**

Moscow, Expocenter

February 8-12, 2016

<http://prod-expo.ru/en/>

Prodexpo is Moscow's largest annual international trade show highlighting high quality foodstuffs manufactured in Russia and Eastern Europe. The exhibition promotes high-quality foodstuffs to the domestic market, giving the opportunity for foreign exporters to present their products and to make valuable contacts. In 2015, Prodexpo hosted more than 2,000 exhibitors from 65 countries and attracted more than 54,000 visitors.

### **Ingredients Russia**

Moscow, All-Russian Exhibition Center (VVC)

March 1-4, 2016

<http://www.ingred.ru/>

Ingredients Russia is the only ingredient exhibition in Russia, a specialized trade show for suppliers and buyers of ingredients worldwide. Ingredients Russia is a key meeting point for all those involved in the Russian ingredients industry. It is an effective way to meet new and existing clients, increase brand awareness and discover the latest news from the Russian ingredients industry. Manufacturers, suppliers and distributors present natural extracts, dietary supplements, flavors and natural ingredients for the production of healthy food and drink products. In 2015, the Expo attracted 5,528 attendees of which 92 percent were key decision makers including food technologists and management of the food processing companies and importers.

If exporters are targeting specific regions within Russia, the Moscow ATO recommends participating in regional exhibitions. Participation fees for regional exhibitions are lower, and are aimed at local consumers and retail food chains. The Russian retail market is competitive; exporters should allocate time to visit Russia and earmark funds in their sales plans for local promotional support. Business relations in Russia depend on personal contacts. For this reason it is important to have a representative office in Russia or to have a well-established contact with a Russian importer. Local partners should be chosen on the basis of references from other foreign exporters or local reputable processing companies. The local partner can help you solve many problems and better understand the peculiarities of the local market that will positively influence the results of your business activities in the targeted market.

Moscow remains the obvious first choice for a representative office in Russia where many food processing companies and representative offices of foreign and regional food companies are concentrated. However, if your contacts are located on the West Coast or will ship through St. Petersburg it might be worth considering St. Petersburg as a home base. Having a representative office in a major Russian city will help you to establish valuable contacts with leading Russian food companies. Moreover, established direct dealership with fast-growing Russian companies will provide

more opportunities to meet customers' demands.

Marketing the products to the buyers and end-users is paramount. Russia's leading processing companies employ qualified personnel and use modern processing technology making them good candidates for training programs for technologists. Also, ingredients suppliers should understand that their clients are actually not ingredients manufacturers but the food products' end-users. Keeping consumers in mind along with the importer/distributor will help U.S. exporters be successful in the Russian market.

## ***B. MARKET STRUCTURE***

Below are three possible ways of working with ingredient processors in Russia.

- Supply products directly to a local food processor;
- Trade via Russian importer/broker to a local food processor; or
- Supply products via a Russian importer/wholesaler to a local food processor.

In Russia, there are a number of large food ingredients importers and distributors. One of the key market trends is concentration of the largest food importers/distributors/processors in Moscow and St. Petersburg, expanding their reach and influence into regions by forcing out and absorbing small local distributors. In the past, there was one key distributor in a Russian region working with all local large processors and small wholesale companies. A few years ago, large Moscow/St. Petersburg-headquartered companies held all distribution channels using their affiliates and partners in the regions.

Russian food processors prefer working through local wholesalers, as wholesalers can offer the whole range of ingredients with attractive discounts. Processors supply their products to wholesalers and also to large food retailers whose share of the market has recently grown. The latest local market trend is a growing demand for high quality food products despite the higher prices. This is a positive sign for foreign ingredient suppliers, as demand for consistently high quality ingredients has been growing leaving far behind locally produced ingredients in terms of their quality. A key task to solve for the exporter along with establishing distribution channels for selling products throughout Russia is a search of an experienced and reputable customs broker who would be able to solve numerous problems and disagreements related to customs.

## ***C. COMPANY PROFILES***

Russian food processors can be divided into the following main groups:

- Large vertically integrated holdings focused on development of their production facilities using their own raw material resources (began in the mid 90s), such as Cherkizovsky meat-processing plant, etc.
- International manufacturers having their production facilities in Moscow or St. Petersburg

suburbs and other large regions of the country, such as DANONE (France), Valio (Finland), Mars (U.S.), Kraft (U.S.), San Interbrew (Belgium), etc.

- Russian holding companies with foreign capital, such as OJSC "Baltika" Brewery Company, KamposMos, and others.
- Regional food processing companies that started their activity under the Soviet times and successfully passed through the period of structural management and production reorganization in the second half of the 90s.
- Small regional producers/entrepreneurs most of whom produce and sell their products in the region where they are located.

The following table includes information about major food processors by category. 21 food processing companies made the list of the 600 biggest Russian companies based on sales volume in 2014. The rating was published by EXPERT rating agency at [www.raexpert.ru](http://www.raexpert.ru).

**Table G. Russia: Company Profiles**

Company (Product types)	Sales in 2014 (\$ Mil)	End-Use Channels	Production Location	Procurement Channels
PepsiCo Russia (non-alcohol drinks, dairy products, snacks, baby food)	\$4,414	Retail, HRI	Russia (>30)	Importers, Direct, Distributors
Nestle Russia (breakfast cereal, baby food, non-alcohol drinks, pet food, coffee, health food, ice-cream, chocolates, candies)	\$2,255	Retail, HRI	Russia (9)	Importers, Direct, Distributors
Baltika Brewery Company (beer, non-alcohol drinks)	\$2,157	Retail, HRI	Russia (10)	Importers, Direct, Distributors
Mars (confectionary, chocolate, ready soups, chewing gum, pet food)	\$2,082	Retail, HRI	Russia (9)	Importers, Direct, Distributors
Coca-Cola HBC Eurasia (non- alcohol drinks)	\$1,903	Retail, HRI	Russia (14)	Importers, Direct, Distributors
Cherkizovo Group of Companies (meat products, sausage)	\$1,796	Retail, HRI	Russia (6)	Importers, Direct, Distributors
Mondelez Rus' (chocolate, biscuits, chewing gum)	1,6223	Retail, HRI	Russia (4)	Importers, Direct, Distributors
EFKO Group of Companies (oils, fats, mayonnaises, ingredients for dairy, confectionary and bakery production)	\$1,590	Retail, HRI, Food Processing	Russia (n/a)	Importers, Direct, Distributors

McDonalds (fast food)	1,370	HRI	Russia (523 restaurants)	Importers, Direct, Distributors
Obyedinyonnye Konditery (confectionary)		Retail, HRI	Russia (19)	Importers, Direct, Distributors
Cargill (glucose syrups, starches, fodder products; meat products)	\$1,108	Retail, HRI, Food Processing	Russia (n/a)	Importers, Direct, Distributors
Danone Russia (Dairy products, yogurts, baby food)	\$1,076	Retail, HRI	Russia (18)	Importers, Direct, Distributors
Sun inBev (beer)	\$957	Retail, HRI	Russia (7)	Importers, Direct, Distributors
Solnichnye Producty (mayonnaises, fat-and-oil products)	\$874	Retail, HRI, Food Processing	Russia (6)	Importers, Direct, Distributors
Heineken United Breweries	\$851	Retail, HRI	Russia (8)	Importers, Direct, Distributors
Ostankinskiy meat processing plant (sausages, semi prepared met products)	\$850	Retail, HRI	Russia (3)	Importers, Direct, Distributors
Moscow-Efes Brewery	\$815	Retail, HRI	Russia (6)	Importers, Direct, Distributors
Russkaya Akvacultura (salmon production)	\$506	Retail, HRI	Russia (n/a)	Importers, Direct
Progress (baby food, mineral water)	\$467	Retail	Russia (1)	Importers, Direct, Distributors
Fazer (bread, bakery products)	\$411	Retail, HRI	Russia (4)	Importers, Direct, Distributors
Syngenta (grain, vegetables, seeds)	\$395	Food Processing, Retail	Russia (n/a)	Importers, Direct, Distributors

#### ***D. SECTOR TRENDS***

##### **Processing Trends**

- Russia's food processing industry had been growing rapidly since 1998 with an annual increase

of 15-25 percent, but regressed as a result of the 2008 financial crisis. The industry is still in recovery mode.

- Due to the food import ban introduced by GOR in August 2014, Russian food processors have to switch to alternative foreign and domestic suppliers of raw materials which results in the quality of the products, additional expenses and increased end-users' prices.
- Weak ruble makes raw materials and ingredients much more expensive which results in increased end-users' prices, lower consumer's demand and decreased sales.
- The food import ban stimulated development of domestic raw materials production and food processing. In 2014, output of the following processed foods increased steadily: vegetable oil, meat and offal, semi-finished meat products, poultry and offals, butter, pasta, sugar, cheese and cottage cheese canned vegetables and mushroom preserves, mineral water.
- The import ban on foreign foods from E.U. and U.S. manufacturers presents a major opportunity for the domestic manufacturers base, and Russian canned food producers have been benefitting, as items such as fresh fruits and vegetables become too costly for many.
- International food processors are very actively investing in the local food processing industry, establishing their own production facilities or acquiring Russian manufacturing facilities in order to reduce overall costs.
- Consolidation among the leading market players. Many Russian food processing companies are interested in forming strategic alliances with foreign partners. The main goals are access to technical knowledge, strengthening the company's image in the market, access to cheaper financing, and personnel training.
- Consolidation in the retail sector resulted in increased power of the retailers who are able to demand more from suppliers in terms of price and fees.
- Lack of developed regional infrastructure and logistical challenges are the obstacles for expansion to remote territories like Volga, Ural, Siberia and Far Eastern regions.
- Russian processors continue to implement new production technologies. Although these changes in the food-processing sector are spurring demand for domestically produced raw materials for further processing, currently Russia is far from meeting the demand for consistently high quality raw materials in the local food-processing sector.
- The growing network of food processing facilities in the regions is spurring demand for high quality ingredients in the regions as well.
- Modern retailing sees rapid development in Russia. The performance and development seen by modern grocery retailing also had an influence on food processing industry. Growing variety of packaged food products available, more active marketing and promotion at the point-of-sale, cheaper prices and increasing consumer preference for the convenience offered by modern grocery retailers.
- Demographic trends influence demand for specific products: the growing population of children in Russia formed favorable conditions for the development of children specific packaged food.
- The convenience trend will have a strong influence on demand. Demand for meal solutions will remain very much dependent on the economic situation in the country and income stability.
- New products remained the driving factor for most dairy categories in 2014. Russian consumers show a desire for new experiences and welcome innovative solutions. This includes products adopting new flavors, forms and packaging.
- Trends in the food products industry reflect those in the specialized ingredients market: growing popularity of innovative dietary products, nontraditional bread varieties with nuts, different seeds, spices, etc., resulting in increased use of high quality and premium food ingredients.

Natural ingredients now capture a greater market share. As a consequence, the market is developing in value terms more than in volume. Major users of micro-ingredients include the following sectors: baking, confectionary, dairy, meat and food concentrates, ice cream sector.

- 86-90 percent of food ingredients as well as chemical raw materials for ingredients production are imported.

## Consumption Trends

Consumers' constantly changing needs and preferences have a significant influence on the food ingredients market. Below are some of the key factors at play:

- Due to decreased purchasing power, consumers' choice mostly depends on the price offered rather than convenience the goods provide.
- FMCG market volume demonstrates 13.6 percent growth; the major factor is increasing average purchase cost.
- As the retail prices significantly increased in the second half of 2014, Russian consumers had to revise their consumption habits and optimize expenditures.
- Consumers favor eating at home which contributes to stable consumption of ready meals and semi-manufactured food.
- Consumers make more conscious choice in favor of food products of higher quality and useful for health in sector of dairy, meat, fish products and confectionary.
- Consumers remain cautious and their purchasing behavior reflects a calculated balance between price and quality.
- Russians are rational and practical/thrifty when making routine purchases. In 2014, consumers felt increase in prices stated optimizing their costs. 28 percent avoid unnecessary spending, 20 percent try to search for products on promotions, 19 percent look for lower prices, and less than 5 percent avoid the temptation to buy unnecessary things.
- Consumers switch to more affordable products: from expensive cheese to cheap processed cheese, from beef and smoked meat to poultry, from fish and seafood to more basic products like poultry, herring, fish and meat cans.
- Consumption of fresh vegetables grows mostly in the category of "borsch set": potato, cabbage and beet.
- Consumers' demand for functional foods is growing and expected to go on growing.
- Russia is an important market in that premium and affordable coexist.
- However, the main factors for consumers are value for money and quality.
- The Russian confectionary market is one of the few where expenditure is ahead of that in Europe. Russians spend about 2.5-3 percent of their incomes on sweets which is higher than in most other developed countries. That said, per capita consumption of sweets is actually lower in Russia than in Western Europe and the United States.
- Baby food is the only sector that had continuous growth even during the financial crisis.
- Russian consumers have started to show more interest in exotic and so called "ethnic" food products like kumis (fermented horse milk) or cheesecake, igniting growth in the use of special flavoring agents.
- Consumers are aware of country of origin and "GMO free" labeling.

- More and more consumers are suspicious of artificial additives and are looking to purchase foods with natural ingredients.
- Low calorie products are becoming more popular, reflecting consumers’ growing interest in health and balanced nutrition.
- Russian consumers are giving more preference to domestically produced (or processed) products because they are perceived as being more “natural” (or healthy) with a national taste and more affordable.
- Russian consumers carefully read product labels.
- Russian food consumers are ready to pay more for branded products, associating them with products of high quality.
- Russian consumers have a negative attitude towards genetically modified products, though their awareness of such products is low and incomplete due to lack of objective information. Genetically modified products tend to be associated with U.S. products.

**SECTION III. COMPETITION**

Local food processors are becoming more and more competitive in terms of quality and consistency that is partially due to government initiatives. For example, according to a long-term social development program for 2020-2030, more than 900 billion rubles (\$29.2 billion) are planned to be invested in the food processing industry, and 55 percent of it is supposed to be used for technological modernization of the industry. The ruble devaluation and food import ban along with the import substitution policy contributed to the development of the domestic food processing sector. At the same time, the GOR is trying to support domestic food producers with protective measures and import quotas in order to make them more competitive. Quantitative quotas and tariff rate quotas (TRQs) are aimed at lowering the share of imported products into the country and strengthening domestic production of commodities.

The details of TRQ policy are available in GAIN reports devoted to poultry and meat products listed in “Other Market Reports” Section.

According to Russian Federal Customs data, U.S. agricultural imports in 2014 totaled \$1.2 billion - 17 percent lower compared to 2013 mainly due to Russia’s food import ban placed in August 2014 and the high exchange rate. The United States was the eighth largest supplier of food, beverages and agricultural products (the same as in 2013) to Russia by value with 3 percent overall market share. The main exporters were Belarus, Brazil, China, Turkey and others. The United States’ top agricultural exports to Russia in 2014 included: soybeans, chicken cuts, food preparations, nuts (almonds, pistachios and peanuts), sunflower seeds, fish and seafood, and other products.

**Table H. Russia: Major Supply Sources for Selected Product Categories by Countries**

Product Category	Major Supply Source in 2014	Strengths of Key Supply Countries
Poultry Meat and Edible Offal (HS Code: 0207) Net Import 528 thousand tons \$801.766 million	Brazil – 34% Belarus – 27% United States – 20%	Brazil and Belarus competes on price, offers favorable terms; U.S. competed in quality, provided technical support, benefits from country-specific TRQ

Pork Fresh, Chilled or Frozen (HS Code: 0203) Net Import 372 thousand tons \$ 1,502.423 million	Brazil – 53% Canada – 21% Chile – 6% United States – 5.6%	Brazil competes on price/credit terms; Canada competed in quality satisfying Russian food processors/sausage manufacturers
Meat of Bovine Animals Frozen (HS Code: 0202) Net Import 531 thousand tons \$ 2,249.478 million	Brazil – 58% Paraguay – 25% Argentina – 4%	Brazil competes on price conditions, long partnership relations with Russia in beef trade
Red Meats Fresh/Chilled/Frozen Net Import 1,163 thousand tons \$4,618.825 million	Brazil – 46% Paraguay – 12% Belarus – 10%	Brazil is leading in price, credit and delivery terms and strong Government support of meat exports
Offal Net Import (HS Code: 0206) 129 thousand tons \$266.493 million	Argentina – 36% Paraguay – 13% Germany – 9%	Argentina offers more competitive prices; Germany has logistical advantages: short shipping time
Fish & seafood (HS Code: 02) Net Import 759 thousand tons \$2,566.070 million	Norway – 22% Chile – 16% China – 12%	Norway enjoyed quality reputation, traditional trade ties, offered strong promotional support, Chile and China compete in price
Soybeans (HS Code: 1201) Net Import 2,028 thousand tons \$1,150.758 million	Paraguay – 46% Brazil – 27% United States – 19%	Paraguay and Brazil are leading in price
Dairy products (excl. cheese) Net Import 867 thousand tons \$2,025.787 million	Belarus – 60% Finland – 5.1% Uruguay – 4.9%	Belarus competes in geographical proximity, balance of price and quality
Cheese and Curd (HS Code: 0406) Net Import 316 thousand tons \$ 1,582.036 million	Belarus – 38% Netherlands – 8% Lithuania - 7%	Belarus competes in geographic proximity and price, Netherlands and Lithuania offered traditionally high quality
Butter, Fats and Oils Derived from Milk (HS Code: 0405)	Belarus – 40% New Zealand –	Belarus competes in geographic proximity and price; New Zealand has reputation for high

Net Import 150 thousand tons \$742.235 million	12% Uruguay – 11%	quality dairy products; enjoys shipments through the Russian Far East
Egg Products (HS Code: 0408) Net Import 719 tons \$ 3.720 million	Argentina – 80% Belarus – 16% Kazakhstan – 1%	Argentina offers more competitive prices
Dried Fruit (HS Code: 0813) Net Import 29 thousand tons \$65.196 million	Turkey – 25% Chile – 24% Argentina – 9%	Major suppliers enjoy traditional trade ties, competitive prices and short shipping time
Nuts (HS Code: 0802) Net Import 37.5 thousand tons \$239.900 million	United States – 50% Iran – 13% Turkey – 12%	U.S. high quality almonds were in growing demand; Iran and Turkey enjoyed competitive prices
Fruit & Vegetable Juice Net Import 237 thousand tons \$410.774 million	China – 21% Netherlands - 15% Brazil – 11%	China competes on price
Sugar, Sweetener, Beverage Bases Net Import 469 thousand tons \$306.220 million	Belarus – 50% China – 12% Moldova – 10%	Belarus competes in geographic proximity and price; China experiences capacities oversupply and offers competitive prices
Protein Concentrates & Textured Protein Substances (HS Code: 210610) Net Import 13.6 thousand tons \$34.437 million	Belarus – 34% China – 20% Serbia – 21 % Korea, South – 8% United States – 7%	Belarus competes in geographic proximity and price; China offers competitive prices and meets processors' requirements in quality
Mixtures of Odoriferous Substances (HS Code: 330210) Net Import 18.6 thousand tons \$439.547 million	France – 32% Ireland – 23% Germany – 19%	European suppliers compete in quality, shipping time and enjoy traditional trade ties.
Lac, Gums, Resins & Other Vegetable Saps and Extracts	India – 21%	India and China offer competitive prices, Germany enjoys traditional trade ties, quality

(HS Code: 13) Net Import 29 thousand tons \$161.257 million	China – 19% Germany – 16% United States – 5%	and short shipping time
Potato Flour, Meal Flakes, Granules, and Pellets (HS Code: 1105) Net Import 12.7 thousand tons \$15.276 million	Germany – 39% Netherlands – 31% Belgium – 11%	Principal suppliers enjoy traditional trade ties, competitive prices and short shipping time
Essential Oils (HS Code: 3301) Net Import 351 tons \$11.271 million	India – 48% United States – 8% Austria – 7%	Principal suppliers enjoy traditional trade ties, competitive prices and short shipping time
Hops (HS Code: 1210) Net Import 2.955 thousand tons \$23.535 million	Germany – 73% Czech Republic – 14% United States – 7 %	Many brew masters are German or German-trained, favor German hops; short shipping time; competitive prices
Dextrins and Other Modified Starches (HS Code: 3505) Net Import 104 thousand tons \$125.626 million	Germany – 19% Netherlands – 17% France – 10% United States – 7.7%	European suppliers compete in quality and short shipping time

#### SECTION IV. BEST MARKET PROSPECTS

In 2014, U.S. agricultural exports to Russia accounted for \$1.2 billion which is 17 percent lower than in 2013, primarily due to the Russia's food import ban placed in August 2014 as well as shrinking demand and high exchange rate. Russia's accession to the World Trade Organization (WTO) has helped to bring some of the country's legal and regulatory regimes closer in line with internationally accepted practices. Also, while Russia's stated goal to be self-sufficient in categories such as meat and dairy products may, to some extent, limit U.S. exports of those products, these goals may also create new opportunities for U.S. exporters to supply high protein feeds and animal genetics.

On August 6, 2014, Russian President Vladimir Putin signed a decree banning a list of agricultural

products from the United States, Canada, European Union, Australia, and Norway as a result of the implementation of economic sanctions against Russia due to events in the region. The ban took place immediately and will remain in place until August 5, 2016. The agricultural products included in the current food import ban are beef, pork, poultry, fruits, vegetables, fish, seafood, cheese, tree nuts and a variety of other products listed by specific HS codes. Once the ban is lifted, ATO Moscow expects the agricultural products listed below will once again be the best sub-sector prospects in the Russian market.

#### **A. Products Present In the Market That Have Good Sales Potential**

- *Soybeans.* The Russian government continues to support the poultry, dairy and pork industries and demand for high protein feeds exceeds Russia's ability to produce them domestically. Soybeans and soybean meal remain one of the most important sources of protein feeds. In calendar year 2014, Russia imported 2.7 MMT of soybeans and soybean meal - 2 MMT of soybeans and 682 TMT of soybean meal in soybean equivalent (533 TMT of soybean meal). Major suppliers in 2014 were Paraguay at 965,000 MT, Brazil at 730,000 MT, the United States at 420,000 MT, Argentina at 283,000 MT, Ukraine at 100,000 MT and Uruguay at 32,000 TMT. Soybean imports are expected to remain at similar levels in 2016 due to the high demand for soybean meal from the expanding poultry and livestock industries in European Russia.
- *Live Cattle and Animal Genetics.* Russia is determined to become self-sufficient in various categories, such as meat and dairy products, and is applying significant resources and market access constraints to make it happen. This opens up new market opportunities for U.S. exporters to supply live cattle and animal genetics. As market access for meat and poultry continues to be limited through the August 2014 food import ban and the imposition of trade-restrictive SPS measures, demand and opportunities for higher quality animal genetics is expected to grow. The highest demand for this category are dairy cattle, specifically registered Holsteins, as well as beef cattle, particularly Black Angus. The Russian government has shown a strong influence in stimulating domestic dairy and beef cattle herd growth. More than 20 billion rubles has been allocated by the Russian government to support beef and dairy projects under new specific sub-programs: "Development of Dairy Cattle Industry and Milk Production" and the "Development of Beef Cattle", and "Development of Purebred Livestock Breeding" in 2015. The main state support programs in livestock sectors are anticipated to remain strong in 2016. The United States exported 16,386 head of live bovine animals to Russia in 2014 valued at approximately \$58 million - the largest supplier of purebred breeding cattle to the country. Market demand also continues to grow for bovine semen and embryos in Russia with many Russian buyers looking to the United States as a supplier. In 2015, the United States exported \$3 million of bovine semen and \$1.5 million of bovine embryos to Russia. The United States is well-positioned to be the major supplier for higher quality animal genetics, especially for producers seeking the best quality for value in the global market.
- *Wine.* Russia is one of the largest global growth markets for wine and is the most developed wine market of all the "BRICs" countries. Italy, France and Spain, the three major wine producers globally, are also the top exporters of wine to Russia. U.S. wine sales were on the rise until 2014 (seeing 20 percent growth annually) but began to slow in 2014 due to the depreciation of the Russian ruble, slowing economy and falling consumer purchasing power. In 2014, U.S. wine sales reached \$13.8 million - down 12 percent from 2013. U.S. wines currently comprise

of 1.2 percent of total market share but there is tremendous opportunity for growth as Russia's wine culture blossoms. Russian wine imports reached \$1.142 billion in 2014. Consumption of wine and sparkling wine in Russia in 2014 surpassed 1 billion liters. Imports of bottled wine account for roughly 30 percent of this volume. Another 40 percent of wine is produced in Russia from imported wine raw materials with only the remaining 30 percent are produced from grapes cultivated in Russia. The highest demand in the Russian market is for low-priced wine products - 70 percent of all wines sell for up to 150 rubles per bottle in retail in 2013-2014. Wine costing up to 300 rubles occupies 15 percent of the market while wine in the 500-ruble range takes up 10 percent. Wine that costs more than 500 rubles per bottle makes up just 5 percent of all wine sales in Russia.

- *Distilled Spirits.* Among the world's top ten spirits markets in volume terms, Russia dramatically increased imports of U.S. bourbon and rum from 2009 to 2013. The United States (including Puerto Rico) is the fourth largest supplier of spirits to Russia and the potential for continued growth is high over the medium term. In 2014, U.S. exports of spirits to Russia totaled \$127 million, down 9 percent due primarily to the depreciation of the Russian ruble which began towards the end of 2014. Total Russian imports of distilled spirits reached \$1.237 billion in 2014, down 17 percent from 2013. All alcoholic beverages saw tariffs fall after Russia acceded to the WTO with full implementation expected by 2016. However, excise tax rates on distilled spirits had increased steadily and significantly from 2011-2014. As a result, it raised the prevalence of illegal vodka in the Russian market that, according to market analysts, accounts for approximately 60 percent in 2014. In 2014, legal domestic vodka production declined by 22.3 percent reaching only 66.6 million deciliters – the lowest level in modern Russian history. Such dynamics led the Russian government to freeze excise taxes on spirits at 500 rubles per liter of anhydrous alcohol for 2015-2016 – the same level as in 2014. Most Russian whiskey lovers are familiar with famous American whiskey and bourbon brands and prefer them to Irish and Scotch whisky products.
- *Processed Fruit & Vegetables.* In 2014, the sales of canned/preserved food in Russia grew by 1.1 percent in volume, frozen processed food sales grew by 6 percent, and chilled processed food grew by 4 percent. Canned/preserved food saw the largest increase in average unit price of any area in meal solutions in 2014 (9 percent). This area is dependent on global prices as Russia is unable to supply sufficient raw materials for canned/preserved vegetables and fruit production. The premium trend is putting upwards pressure on prices as well. However, the increase in average unit prices seen across all meal solution areas was mainly in line with inflation. In the canned products sector, even for those branded products that maintain a strong presence in chained retailers, the competition will become significantly more intense due to developing of private label products in terms of marketing and shelf positioning.
- *Condiments and Sauces.* In 2014, the sales of sauces, dressings and condiments grew by 1 percent in volume in Russia. (Source: Euromonitor International) The U.S. share of the sauces and mixed condiments accounted to more than \$5 million representing a 6 percent growth in 2014. The market is positively influenced by the development of Asian consumer food service, with the retail market for packaged Asian food recording stable annual growth especially in sauces. Many sauces producers offer a variety of oriental flavors responding to consumer preferences. In addition, herbs and spices also gained a number of customers aware of Asian spices like curry and various spicy flavors. Sauces, dressings and condiments are one area where multinational brands dominate over domestic producers. Demand for such products in Russia is growing which provides great opportunities for U.S. suppliers. Sales will be driven by

population growth and new product development which will be supported by active promotion and advertising provided by the growing retail sector.

- *Snack Foods*. Snack foods are gaining popularity in Russia. Sales growth is being fueled by growing impulse and indulgence product assortments as well as the shift amongst consumers to more premium products, especially in areas like industrial cakes, chocolate confectionery and snack bars. New product development, especially in snack bars and ice cream is making people eager to try new products and stimulating sales growth. As a result of growing concerns about healthy food, snack bars are recognized as healthy alternatives to chocolate snacks nevertheless snack bars are relatively new in Russia. Due to the popularity of novelty snack bars, sales growth is fastest in impulse and indulgence products, with current value sales rising by 19 percent in 2014.
- *Hops*: Rapidly expanding sector relies heavily on imports from Europe; very limited local commercial production.
- *Rennet casein*: The replacement of rennet cheeses which is not available at the moment from the EU can be rennet casein: it can completely replace rennet cheese or cottage cheese in the production of all types of processed cheese.
- *Milk protein concentrate*: Given the shortage of raw milk, milk protein concentrate is becoming increasingly popular.
- *Lactose*
- *Flavor enhancers* for processed meat products
- *Natural sweeteners and colorants*: Healthy eating trend conditions using natural ingredients in food processing.
- *Sugar, sweeteners and beverage bases*.
- *Functional soy concentrates and isolates* (primarily for sausage production)
- *Butter, milk powder*
- *Quality Textured Vegetable Protein*
- *Gluten Powder*
- *Dextrin and other modified starches*
- *Complex ingredients* including colorants, sweeteners, emulsifiers and preservatives.
- *Frozen or soft pasteurized fruits* – for yogurt and ice cream production.

#### **B. Products Not Present in Significant Quantities but Which Have Good Sales Potential**

- Specialized food ingredients, including carrageenan, emulsifiers, enzymes, pectin, starter cultures, and functional systems (integrated blends of emulsifiers and thickeners)
- Certified organic/natural ingredients: while many local processors are advertising “natural” or “ecologically-clean” food and beverage products, there are no official organic standards and such claims cannot be substantiated.
- Kosher and halal-certified ingredients (sizable Jewish population with growing interest in kosher products; large Moslem consumer base in Russia and CIS counties).

#### **SECTION V. POST CONTACT AND FURTHER INFORMATION**

Contact Information for FAS Offices in Russia and in the United States

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Email: [atomoscow@fas.usda.gov](mailto:atomoscow@fas.usda.gov)

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Tatyana Kashtanova, Administrative Assistant

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American Embassy

Bolshoy Devyatinskiy pereulok, 8

121099 Moscow, Russia

Tel: 7 (495) 728-5560

[www.usfoods.ru](http://www.usfoods.ru)

*For mail coming from the U.S. (delivery may take 2 to 4 weeks):*

Director, Agricultural Trade Office

5430 Moscow Place, Box 355

Washington, DC 20521-5430

*Covering Northwest Russia (St. Petersburg):*

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*For General Information on FAS/USDA Market Promotion Programs and Activities:*

Office of Trade Programs  
U.S. Department of Agriculture  
Foreign Agricultural Service  
1400 Independence Ave., S.W.  
Washington, DC 20250  
[http://www.fas.usda.gov/OTP\\_contacts.asp](http://www.fas.usda.gov/OTP_contacts.asp)

FAS Website: [www.fas.usda.gov](http://www.fas.usda.gov)

*For Trade Policy/Market Access Issues, General Information on the Russian Agricultural Sector, etc.:*

Jonathan P. Gressel, Agricultural Minister-Counselor  
Robin Gray, Senior Agricultural Attaché  
Rachel Vanderberg, Agricultural Attaché  
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*Other Useful Contacts*

The Agricultural Trade office works with a large number of U.S. industry organizations, several of which are resident in Russia. These cooperators share the view that Russia is a promising market for food products.

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[www.alaskaseafood.ru](http://www.alaskaseafood.ru)

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<http://www.usapeec.ru>

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Wine Institute of California

Olga Tuzmukhamedova

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E-mail: [olgatuz@mail.ru](mailto:olgatuz@mail.ru)

<http://www.discovercaliforniawines.com/>

The American Chamber of Commerce is another good source for information on doing business in Russia. The Chamber has offices in Moscow and St. Petersburg.

American Chamber of Commerce in Russia (AmCham)  
Ul. Dolgorukovskaya, Building 7, 14th floor  
127006 Moscow, Russia  
Tel: 7 (495) 9612141  
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<http://amcham.ru/>

American Chamber of Commerce in St. Petersburg  
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Email: [all@spb.amcham.ru](mailto:all@spb.amcham.ru)  
<http://amcham.ru/spb/>

The U.S Commercial Service has offices in Moscow and St. Petersburg. For questions regarding agricultural machinery, food processing and packaging equipment or materials, refrigeration equipment, and other industrial products, please contact:

U.S. Commercial Service  
Bolshoy Devyatinskiy pereulok, 8  
121099 Moscow, Russia  
Tel: 7 (495) 728-5580  
E-mail: [Moscow.Office.Box@trade.gov](mailto:Moscow.Office.Box@trade.gov)  
<http://export.gov/russia/>

The U.S. Commercial Service office at the U.S. Embassy in Moscow assists American exporters by identifying potential partners through the Gold Key Matching Service. The program features:

- appointments (typically four per day) with prescreened Russian firms;
- background and contact information on each potential partner, such as: the size of the company; number of years in business; product or service lines; and capability to provide after-sales service;
- customized market briefing with U.S. Commercial Service staff; and,
- available market research on the relevant industry sector.

### **Other Relevant Reports**

Attaché reports on the Russian food and agricultural market are available on the FAS Website; the search engine can be found at  
<http://gain.fas.usda.gov/Lists/Advanced%20Search/AllItems.aspx>

[RS15100 Food and Agricultural Import Regulations and Standards - Narrative](#)

[RSATO026 Exporter Guide](#)

[RFATO 028 Retail Report / Annual](#)

[RSATO040 Russian Food Processing Sector](#)

[RSATO Russian HRI Sector](#)

[RFATO025 Fresh Deciduous Fruit / Annual](#)

[RFATO005 Consumer Trends in Food and Retail Sector](#)

[RSATO006 Russian Retailers Modify Strategies as Economy Slows](#)

[RFATO001 Food Import Ban Changing Russian Far East Food Market](#)

[RSATO1109 Russian Organic Market](#)

[RS1561 Livestock and Products Annual Report](#)

[RS1512 - 2015 Livestock and Products Semi-annual](#)

[RS1527 Fish and Seafood Production and Trade Update](#)

[RS1554 Poultry and Products Annual](#)

[RS1599 GOR Distributes Meat and Poultry TRQs for 2016](#)

[RS1547 July 2015 Grain and Feed Update](#)

[RS1530 2015 Dairy and Products Semi-annual](#)

[RSATO 1205 Strategy of the Russian Food Industry Development until 2020](#)

[RS1584 Dairy and Products Annual Report](#)

[RS1582 Draft Rules of HACCP Implementation in Russia](#)

[RSATO1208 Customs Union Technical Regulations on Food Products Labeling](#)

[RS1233 Customs Union Technical Regulation on Food Safety](#)

[RS1250 Customs Union Technical Regulation on Safety of Grain](#)

[RSATO1211 Customs Union Technical Regulations on Food Products Labeling](#)

[RS1326 Customs Union Technical Regulation on Fat and Oil Products](#)

[RS1334 Customs Union Technical Regulation on Juice](#)

[RS1340 Customs Union Technical Regulation on Specialized Foods](#)

[RS1338 Customs Union Technical Regulation on Food Additives](#)

[RS1253 Customs Union Technical Regulation on Safety of Packaging](#)

[Customs Union Technical Regulation on Milk and Dairy Products – RS1382](#)