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GAIN Report

Global Agricultural Information Network

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Russian Federation

Food Service - Hotel Restaurant Institutional

HRI Sector Adapting to Slowing Economy and Ruble Depreciation

Approved By:

Erik W. Hansen

Prepared By:

ATO Moscow Staff

Report Highlights:

With the slowing economy and weak ruble, the Russian food service sector has made some shifts of customers from expensive restaurant formats to casual places, from casual dining to fast casual format, and from quick service restaurants to retail ready food with affordable prices. The devaluation of the ruble in 2015 has had a relatively positive impact on hotels in Russia. Foreign visitors have benefited from the ruble depreciation and domestic travel has served as a main driver of growth in the industry. In the first three quarters of 2015, Russia experienced double-digit growth in hotel occupancy. This provides ample opportunities for U.S. exporters of food and agricultural products.

Post:

Moscow ATO

Author Defined:**Executive Summary:**

The restaurant sector in Russia has faced a number of serious challenges in 2014-2015: a food import ban placed on numerous countries in August 2014, a smoking ban in restaurants and bars, weakening ruble, currency fluctuations, and dropping consumer purchasing power. Nevertheless, chained fast food restaurants recorded a 29 percent growth in value sales and increased its number of outlets by 16 percent, making franchising the key expansion method for foodservice chains in Russia. American fast food formats dominate in Russia. Today foodservice market sees some shift of customers from expensive restaurant formats to casual places, from casual dining to fast casual format, and from quick service restaurants to retail ready food with affordable prices. The devaluation of the ruble in 2015 has had a relatively positive impact on hotels in Russia. Foreign visitors have benefited from the ruble depreciation and domestic travel has served as a main driver of growth in the industry. In the first three quarters of 2015, Russia experienced double-digit growth in hotel occupancy and in Revenue per Available Room.

SECTION I: MARKET SUMMARY

At the end of 2014, the Russian economy slipped into recession, which was marked by a combination of several factors: significant limitation of capital inflows (investment, credits), import restrictions, falling oil prices and the devaluation of the ruble. The main factor in the current slowdown is the decline in consumption, under the influence of sustained contractions in real wages. Further decreasing domestic demand is expected to slow down inflation, which is expected to halve in 2016.

According to the Russian Federal Statistics Service (Rosstat) data, Russia's gross domestic product (GDP) grew a meager 0.6 percent in 2014 compared to 1.3 percent in 2013 and fell 3.6 percent in first half of 2015 due primarily to low global oil prices which is the main driver of the Russian economy. Unemployment was at record lows 5.2 percent in 2014 (5.5 percent in 2015). The real salary of Russians in January-October 2015 dropped by 9.3 percent compared to the same period of last year. Today, it is almost the same salary in dollar terms as it was 10 years ago. Inflation in Russia in 2014 rose by 11.4 percent, its highest level since 2008. From January - October 2015, inflation totaled 11.21 percent. Russia has faced a number of serious challenges since autumn 2014. A food import ban from numerous countries announced in August 2014, a weakening ruble, dependent of oil prices, which declined to their lowest level since 2010, currency fluctuations, and high inflation have dropped consumer purchasing power.

Table 1: Russia: Social and Economic Key Figures

	2010	2011	2012	2013	2014	2015* forecast
Population, million.	149.2	143	143.3	143.7	146.3	146.3

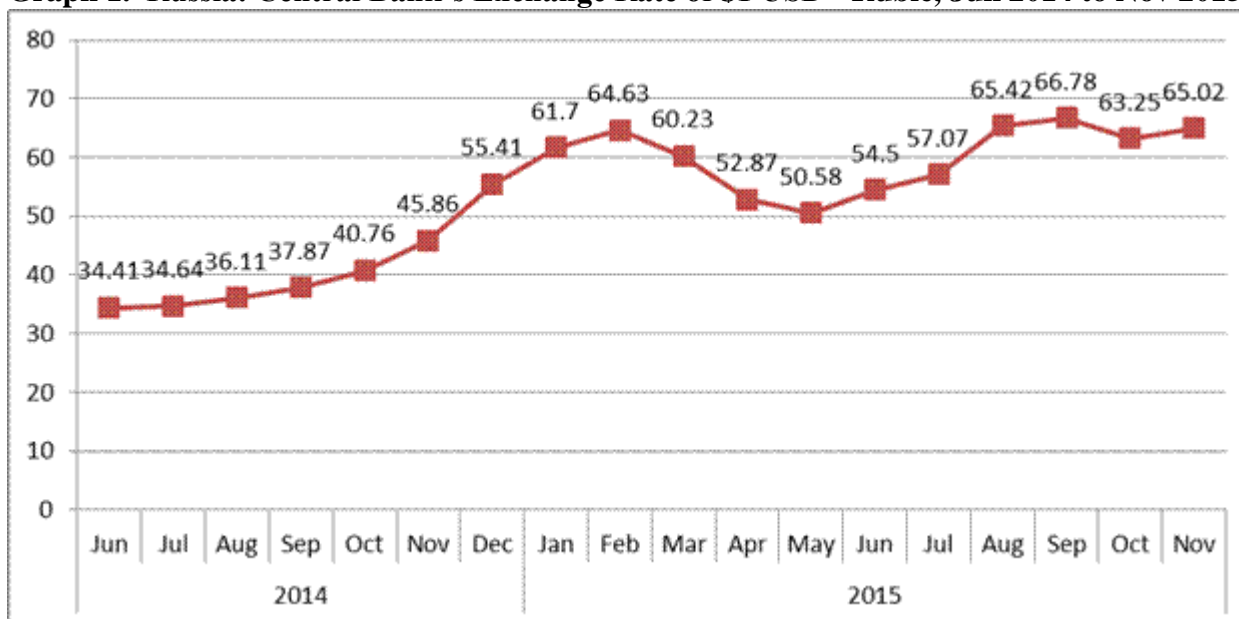
Unemployment, % of labor force	7.3	6.5	5.5	5.5	5.2	5.5
Average monthly salary per person, RUR	20,952	23,369	26,629	29,792	32,611	32,911
Real GDP growth, % change y-o-y	4.5	4.3	3.4	1.3	0.6	-3.7
Inflation, %	8.8	6.1	6.6	6.5	11.4	12-13
Exchange rate (per \$1)	30.36	29.35	31.07	31.9	39.34	60.49

Source: Federal State Statistics Service (Rosstat)

*Forecast for 2015

Russia is very dependent of oil prices, which declined to their lowest level since 2010, putting substantial depreciation pressure on the Russian ruble. Since the beginning of 2014, the ruble has depreciated by almost 100 percent against the dollar. The ruble fell to 66.73 rubles/USD and 70.65 rubles/euro on December 1, 2015.

Graph 1. Russia: Central Bank's Exchange Rate of \$1 USD - Ruble, Jun 2014 to Nov 2015



Source: Central Bank of Russian Federation

According to Russian President Vladimir Putin's Decree on August 6, 2014, imports of a long list of meat, fish, fruit, vegetables, and dairy products were restricted from the United States, European Union, Australia, Norway, and Canada in retaliation for the application of Western economic sanctions. Iceland, Montenegro, Albania and Liechtenstein were added to the list of affected countries in August 2015 and Ukraine will be added if an economic agreement is signed between Kiev and the European Union as is planned.

In 2014 food price inflation hit 15.4 percent, driven up by the declining value of the ruble and Russia's ban on many food products from the United States and European Union. Food price inflation for 10 months of 2015 reached 15 percent. Food price rises have been key factor behind inflation, but it has also been driven by steady devaluation of the ruble. Rising inflation, higher food prices, a weakening ruble, and falling consumer purchasing power is leading many Russians to lessen visits to restaurants

and to switching from higher level restaurants to more affordable restaurants such as fast food type establishments.

HRI Sub-Sectors

Restaurants

According to the Russian Federal Statistics Service (Rosstat), turnover of restaurants and cafes in Russia grew by 8.3 percent to 1.225 trillion rubles in 2014. In the first ten months of 2015, turnover of restaurants, cafes and bars fell by 5.9 percent to 1.046 trillion rubles in comparison to the same period of 2014. The decline of different foodservice sectors differs with fast food being the most popular and fastest-growing sector in Russia. This makes places fast food in a better situation in comparison to fine dining and mid-range restaurant.

Table 2. Russia: Food Service Industry Sales, in Rubles

	2010	2011	2012	2013	2014	January- October 2015
RUR, billion	781.4	903.6	1019.6	1,131	1,225	1,046
Growth Year on Year, %		15.6	12.8	10.9	8.3	-5.9
US Dollars, billion	25.63	30.77	32.62	35.54	31.15	17.29
Average exchange rate	30.48	29.35	31.07	31.82	39.34	60.49
Inflation rate	8.8	6.1	6.6	6.5	11.4	15.6

Source: Federal State Statistics Bureau (Rosstat), Central Bank of Russia

According to Rosstat, as of January 1, 2015 the population of Russia amounted to 146.3 million people. European Russia, geographically west of the Urals, hosts more than 68 percent of the total population, although it accounts for only 21 percent of the country's territory. 74 percent of all Russians lived in urban areas and about 12 percent of the total population lived in Moscow (12.197 million people) and St. Petersburg (5.191 million people). Beyond the two largest Russian cities there are thirteen cities (Novosibirsk, Nizhniy Novgorod, Yekaterinburg, Samara, Omsk, Kazan, Ufa, Chelyabinsk, Rostov-on-Don, Volgograd, Perm, Krasnoyarsk, and Voronezh) with a population of more than one million people.

Currently the largest cities in Russia, Moscow and St. Petersburg, account for 41 percent and 15 percent respectively in terms of chain outlets on the overall consumer foodservice market. Moscow and St. Petersburg remain the leaders in HRI concentration and growth as well as the industry trend-setters. These two cities control 14 percent of Russian foodservice market. High operational costs in Moscow and St. Petersburg, and the fact that the foodservice market in both cities is highly saturated, are forcing the main players to consider regional expansion in order to sustain their share. The foodservice market in the regions of Russia is still relatively underdeveloped and has strong potential for further growth.

Franchising and sub-franchising has become a very popular tool for multinational and local players in Russia. Franchising offers an easier way for investors to enter the Russian market with a lower level of investment, since the materials required for the setting up of outlets and apparatus are often included as part of the franchise agreement, cutting expenses and bringing about profits more quickly.

The significant political and economic changes that appeared in 2014 led to the population and consumer foodservice operators focusing more on Russian cuisine. After the food embargo, major

industry players started to search for new domestic product suppliers to compensate for the lack of imports from Western countries. The majority of consumer foodservice operators have faced considerable difficulties in the development of their import-substitution programs, due to the fact that a lot of produce was manufactured only in particular Western countries and did not have an analogue in Russia. Such a situation is extremely difficult, especially for the full-service restaurants category, where menus strongly depended on Western supplies. However most of restaurants were able reorient their business on domestic suppliers, and very often menu concepts of local foodservice chains have based on Russian cuisine. Market analysts report an average check totals drop by 10-30 percent because of significant traffic reduction. Mid-range restaurants with average check up to 2,000 rubles are the ones feeling the biggest drop in clientele while the lower cost (fast food) style restaurants are still doing good business.

Major Restaurant Operators in Russia

According to Euromonitor International, the number of cafes, restaurants, and other food outlets in Russia currently stands at about 893,000 and almost 82 percent of outlets are independent (non-chain) cafes and restaurants. RBC Research shows that there are currently more than 470 restaurant chains operating in Russia of which 140 of the chains are operating on franchise. The current total number of chained restaurants totals 14,773, of which 7,058 are franchisees, making the share of this group 48 percent. McDonald’s, Subway, Rosinter Restaurant Holding, Arkadiy Novikov Restaurants, Ginza project, Markon, Shokoladnitsa are the largest restaurant chains in different foodservice segments in Russia.

Table 3. Russia: Consumer Foodservice by Independent vs Chained Outlets, 2014

Outlets	Independent	Chained	Total	% of Total
Fast-food	18,064	8,340	26,404	28.5
Street stalls/kiosks	11,240	1,772	13,012	13.8
Cafés/bars	9,675	1,905	11,580	12.4
Full-service restaurants	5,509	1,555	7,064	7.6
Pizza consumer foodservice	3,471	726	4,197	4.5
Self-service cafeterias	29,520	136	29,656	31.7
100% home delivery/takeaway	610	825	1,435	1.5
Total	78,089	15,259	93,348	100

Source: Euromonitor International

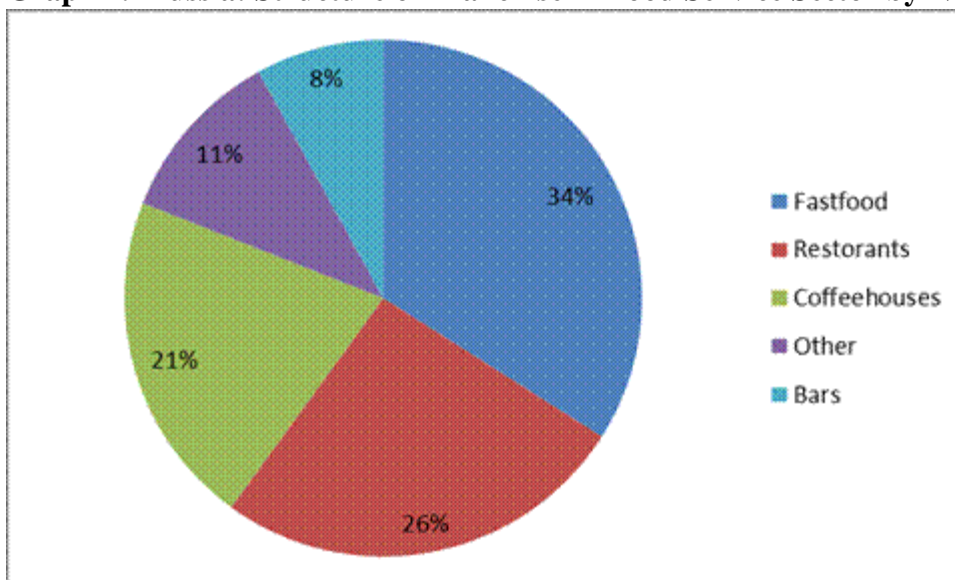
The Russian restaurant market can be broken down into the following segments:

- Fine-Dining/Full-Service Restaurants: higher priced/exclusive outlets;
- Casual-Dining Restaurants: affordable, family dining outlets;
- Quick and Casual Restaurants, which include coffee shops
- Fast-food/Quick Service Restaurant (QSR), which is divided into two separate segments:
- Stationary fast-food and street/mobile fast food (kiosks, stalls, etc.)

Three main segments of the market stand out clearly. The highest-priced segment, “fine-dining” in Western terminology, has an average check of roughly \$70 per person. Patrons receive refined cuisine, unique design, good service, and the availability of private dining space. The medium-priced or casual segment has an average check of \$20 to \$70 per person, and it includes chains such as Il Patio, Chayhona, Goodman, and Planet Sushi. The lowest-priced segment, fast-food, mainly consists of chains such as McDonald’s, Subway, Burger King, KFC, and Kroshka-Kartoshka.

Chained fast food restaurants recorded a 29 percent increase in value sales, one of the highest category sales rises of 2014, and rapidly developed its presence through increasing its number of outlets by 16 percent, making franchising the key expansion method for foodservice chains in Russia.

Graph 2. Russia: Structure of Franchise in Food Service Sector by Number of Concepts



Source: Francon, Franshisa.ru

Table 4. Russia: Leading Foodservice Restaurant Companies by # of Outlets, July 2015

Holding company	# Outlets	% Growth y-o-y	Brands	Type
Markon	828	-8.5	Stardog!s, Bageteria	Street + QSR
Subway	670	-5.8	Subway	QSR
Galereya Alex	542	37.3	Shokoladnitsa, Vabi Sabi	QSR + casual
McDonald’s	517	17.3	McDonald’s, McCafe	QSR
Kroshka-Kartoshka	388	-22.8	Kroshka-Kartoshka	Street + QSR
Yum!Brands	358	34.2	KFC, Pizza Hut	QSR
BRPI	327	22	Baskin Robins	QSR
Rosinter	325	-8.7	Il Patio, Planet Sushi, other	Casual
Burger King Rus	290	29.4	Burger King	QSR
G.M.P. Planeta Gostepreimstva	272	-4.8	Sbarro, Vostochnyy bazar, Yolki-Palki, Yam Kee	QSR + casual

Mega Group	149	1.4	Cinnabon, Hesburger, Aunte Anne's	QSR
Ginza Project	134	15.5	Yaposhka and different concept restaurants	Fine + casual
Novikov Group	105	19.3	Different concept restaurants	Fine + casual+ QSR

Source: FoodService magazine 2015, company's web-sites

Table 5. Russia: Leading Foodservice Brands, July 2015

Brand	# Outlets, Corporate	# Outlets, Franchised	Holding Company	Type	Country of origin	Year Est. in Russia
Stardog!s	-	828	Markon	Street + QSR	Russia	1993
Subway	3	667	Subway	QSR	USA	1994
McDonald's	515	2	McDonald's	QSR	USA	1990
Shokoladnitsa	415	97	Shokoladnitsa	QSR + casual	Russia	2001
Kroshka-Kartoshka	240	148	Kroshka-Kartoshka	Street + QSR	Russia	1998
Baskin Robins	10	317	BRPI	QSR	USA	1992
KFC	113	245	Yum!Brands		USA	1993
Burger King Rus	287	3	Burger King	QSR	USA	2010
Sbarro	127	23	G.M.P. Planeta Gostepreimstva	QSR + casual	USA	1997
Il Patio	76	69	Rosinter	Casual	Russia	1993
Cinnabon	6	101	Cinnabon	QSR + casual	USA	2009
Planeta Sushi	61	58	Rosinter	Casual	Russia	1999

Source: FoodService magazine 2015

Table 6. Russia: Leading Franchises in the Russian Market 2014-2015

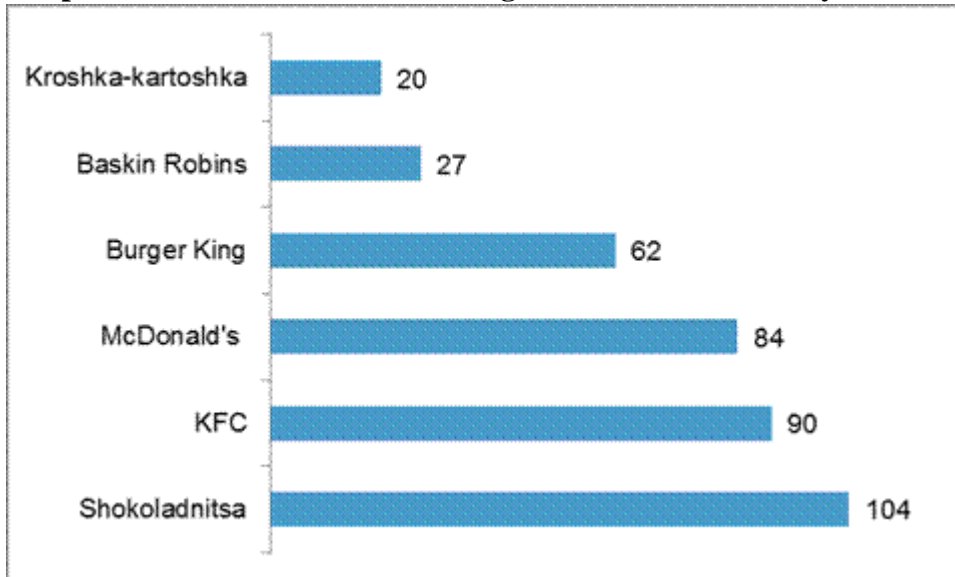
Holding company	Brand	Type	# outlets own/franchise	Geography	Lump sum payment/Royalty
Mega Group	Cinnabon	Bakery	/more than 100	50 Russian cities	\$18000/6%
	Hesburger	Burger	/more than 40		10000 euro/6%
Coffee Set	CoffeeShop Company	Coffee house	50/35	16 Russian cities	28500 euro (1euro=50Rub)/6%
Double B Coffee&Tea	Double B	Coffee house	23	4 Russian cities, Kazakhstan,	1 mln. Rub for Moscow and 800000 Rub. for

				Prague	regions/0%
NF Rus	Nathan's Famous	Hot dogs	/11	Moscow, Sochi, Novorossiysk	\$6000/6%
3 Papas LLC	Papa John's	Pizza	39/23	15 Russian cities, Belarus, Azerbaijan	\$35000/7.5%
Subway Russia Franchising Company	Subway	Sandwich	/more than 690	150 Russian cities	\$7500/8%
Traveler's Coffee	Traveler's Coffee	Coffee house	80/16	40 Russian cities, China, Ukraine, Kazakhstan, Azerbaijan	1.5 mln. Rub/3%
Yum! Restaurants International Russia & CIS	KFC	Fast food	/347	10 Russian cities & CIS	\$47700/11%
Markon	Stardog's	Street food	40/800	70 Russian cities	30000 Rub/3-5%
Shokoladnitsa	Shokoladnitsa	Coffee house	417/88	100 Russian cities, Kazakhstan, Ukraine, Azerbaijan	\$70000/7%
G.M.P. Hospitality Planet	Sbarro	Pizza	126/27	50 Russian cities, Kazakhstan, Azerbaijan	\$24900/7%
	Yolki-Palki	Russian cuisine	23/28	11 Russian cities	2 mln. Rub/6%
	Yam Kee	Noodles	25	7 Russian cities	\$12900/5%
	Vostochnyy Bazar	Asian cuisine	43/13	20 Russian cities	\$14900/6%
Rosinter Restaurants Holding	Planet Sushi	Japanese cuisine	61/58	40 Russian cities,	35000 euro/6%
	Il Patio	Italian cuisine	76/69	Moldova, Belarus, Ukraine, EU	

Source: Russian Franchising Association

Food service operators take certain steps to increase interest of private capital to their brands. One of the main ways to help its franchisees in 2014-2015 is reduction of the lump sum payment (one-time payment of the new owner of the shop to franchisor for the entrance to the market under the known trade mark) and royalty, as well as transfer payments between franchisor and franchisee from hard currencies to rubles.

Graph 3. Russia: Growth of Leading Foodservice Brands by # of Outlets, Jul 2014 – Jul 2015



Source: FoodService magazine June 2015

Fine-Dining/Full-Service Restaurants

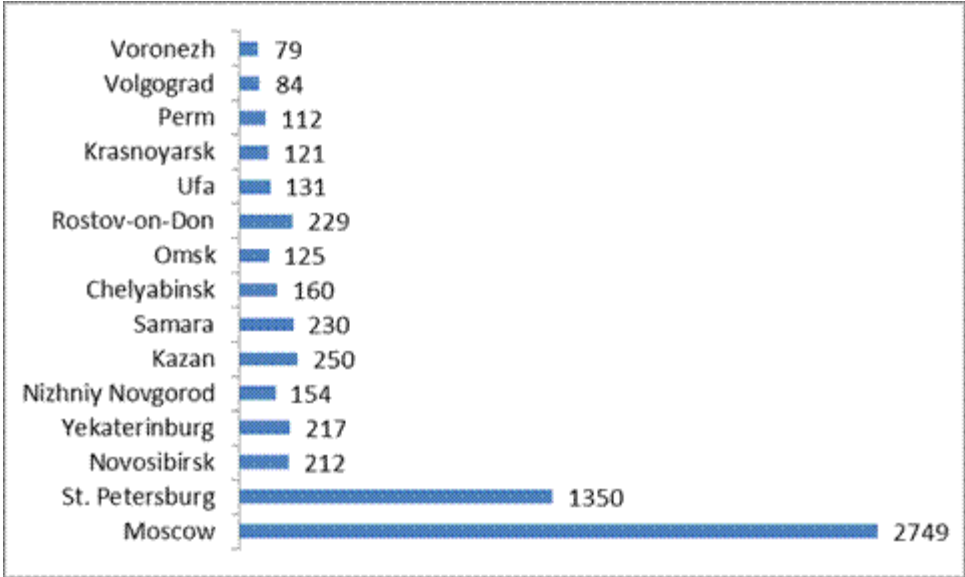
In 2014, full-service restaurants became the most negatively affected category within Russian consumer service. By the end of the year it generated a 4 percent decrease in its number of outlets and stood out for its considerably lower annual value sales. Haute cuisine appeared in Russia in the mid 1990's, and there is no shortage of high-end restaurants with extravagantly expensive checks at meal's end in Moscow and St. Petersburg. Fine-dining restaurants are associated with names such as Arkadiy Novikov, Andrey Delos, and Ginza Project, but most experts agree that the top-category restaurant sector is saturated. Restaurateurs are moving toward casual restaurants where tables turn over more quickly and profit margins are higher. Nevertheless, there is still an opportunity for U.S. products in the fine dining segment because consumers are loyal to high-quality imported products such as marbled beef, seafood as soon as food embargo would be lifted, high-end wines, and spirits.

Ginza Project is one of the largest consumer foodservice businesses in Russia. The company operates various restaurants and entertainment venues with different formats and price segments, although there is a bias towards various fine dining options. The restaurant holding Ginza Project began developing a nationwide network of Yaposha cafés in 2003. Since 2008, Ginza Project has continued to invest heavily in its expansion. The group opened its themed restaurants in Moscow, St. Petersburg, Rostov-on-Don, and New York. As of December 2015, the company operates 134 outlets, including 76 fine-dining restaurants in Moscow and St.Petersburg. Currently company has focused on development democratic restaurant Paul's bakery shops and restomarket project ObedBufet.

Arkadiy Novikov Restaurant Group (Novikov Group) includes more than 100 restaurant-retail-entertainment projects of various formats and price ranges. The company has launched and managed restaurants since 1992 and has continued to place second in full-service restaurants. The Novikov Group is slightly less chain-oriented. It operates more than 50 different Moscow high-end concept restaurants, along with a casual-dining restaurant chains such as, Sushi Vesla, Prime Star, and Kish-Mish. It also operates the premium grocery chain Globus Gourmet, the Russian branch of the French gourmet chain Hediard, the greenhouse complex OOO Agronom, and the Premium Class catering business. Novikov has also branched out internationally and has four restaurants in London named Novikov Restaurant and Bar. Since 2013 Company has developed Krispy Kreme doughnut café chain.

According to 2GIS Research, as of March 2015, the amount of fine-dining and casual restaurants in the 15 largest Russian cities totaled 6,203 in number. The total number of Moscow foodservice outlets in the 15 largest cities reached 10,303 (3481 cafes, 2,749 restaurants, 2,318 fast food, 1,123 bars, 897 coffee houses, 500 other formats).

Graph 4. Russia: Fine-dining and Casual Restaurants in 15 Largest Cities, March 2015



Source: 2GIS

Casual-Dining Restaurants

The leading position in this segment belongs to the chain operators, including those specializing in Russian, North American, Italian, and Asian cuisines. The poor development of independent operators across most full-service restaurant formats means it is heavily concentrated with chains, especially in Moscow and St. Petersburg. Independent restaurants face strengthening competition from cafés, bars, and fast-food outlets, which provide good quality food at lower prices. Russian consumers prefer a diverse menu at affordable prices. The average price for a meal at one of these restaurants ranges from \$20 to \$70 per person.

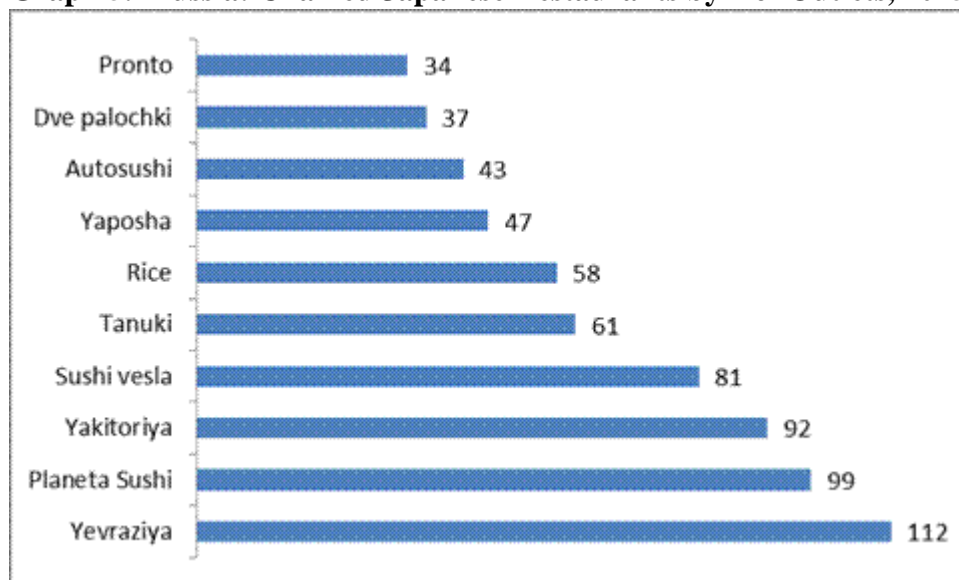
North American-style steakhouses, Japanese cuisine, and European restaurants are very popular in Russia. More than 50 percent of the food it serves up is imported. Some hard to replace items like French and Italian cheeses, Norwegian salmon, Australian ribeye steak, Finnish butter and even cheap

American drumsticks, and seafood are heading off the menu at restaurants after the ban on imports of all fish, meat and dairy produce. This is extremely difficult situations for the fine dining and even mid-range restaurant which serves sushi, seafood and have European menus.

Although meat dishes are a staple of almost every Russian restaurant, North American-style steakhouses are not yet widespread, accounting for only 3 to 4 percent of the Moscow market. Experts attribute this to the fact that opening a steakhouse cost 15 to 20 percent more than opening the average restaurant, due to the need for special grilling equipment and a downtown location to attract a profitable number of customers. Rent is significantly higher in the city center than in the suburbs. Currently, the main American-cuisine restaurants in Moscow are the American Bar & Grill chains (operated by Rosinter), Chicago Prime, twelve Goodman steakhouses (operated by RP-Com), Louisiana Steakhouse, and ten Torro Grill restaurants. Even though the number of steakhouses is growing, overall consumption of steaks is increasing steadily. Currently these restaurants use local meat due the ban, although local suppliers do not provide consistent quality.

The enormous popularity of Japanese cuisine made Asian full-service restaurant chains the most ubiquitous category of casual restaurants. Japanese restaurants, with sushi and fish menus, are heavily represented among fish and seafood-concept restaurants in Russia. Currently Japanese restaurants are in difficult situation due to Russian food ban. It's difficult to find substitutions of Norway salmon. After the August 2014 ban suppliers of salmon from Chile and the Faroe Islands to Russian have almost doubled their prices and as a result Japanese restaurants are expensive and less popular now. In September 2014, a popular sushi chain Yevraziya, closed 10 outlets in its home city St. Petersburg, and sold off all 15 of its restaurants in Moscow. One of Yevraziya's owners says his chain is being squeezed from two sides: Russian sushi lovers have less money to spend, and the price of supplies has skyrocketed.

Graph 5. Russia: Chained Japanese Restaurants by # of Outlets, 2015



Source: RBC

Very few casual chain restaurants have a centralized system of purchasing. Most decisions regarding products and purchasing are made at the restaurant/group level. On the one hand, there are many more

opportunities for sales, since each restaurant is a separate account. On the other hand, individual sales are smaller and do not allow for the development of exclusive distribution rights and consistent volumes. After the food import ban went into place in August 2014, Russian restaurateurs have been trying to use as much local products as possible and are developing Russian, Soviet, Georgian and Uzbek cuisine. Most casual eateries in Russia, before the ban, used imported meat, seafood, desserts, seasonings, and a variety of ingredients and liked it because of the high quality for price ratios.

Rosinter Restaurants Holding (Rosinter) is a major player on the Russian restaurant market. The company gained its leadership role by its early deployment of chain restaurants in the casual-dining segment of the market where Rosinter held 325 outlets in Russia, the CIS, Central Europe, and the Baltic states. Rosinter revenue in the first half of 2015 decreased by 18.9 percent and stood at 3.8 billion rubles year-on-year due to restaurant portfolio optimization and reducing the number of transactions. The company offers Italian, Japanese, American, and Russian cuisine under its proprietary brands (Il Patio, Planet Sushi, American Bar & Grill, Mama Rasha and Shikari) and its licensed brands (T.G.I. Friday's, Costa Coffee, and McDonald's). Il Patio and Planet Sushi are among the most recognized brands in Russia, and recently company launched new pan Asian restaurant concept Shikari. Around 15 million guests a year visited Rosinter's outlets in 2014.

Table 7. Russia: Rosinter Restaurant Brands, September 2015

Brand name	Type	Start of operation in Russia	# outlets, Corporate	# outlets, Franchised
Planet Sushi	Casual (Asian)	1999	62	44
Il Patio	Casual (Italian)	2004	75	67
T.G.I. Friday's	Casual (American)	1997	24	-
American Bar & Grill	Casual (American)	1994	8	-
Costa Coffee	Coffee house	2008	30	1
Other			18	
Total			210	115

Source: Rosinter data

Table 8. Russia: Rosinter Consolidated Revenues in 2009-2014

	2009	2010	2011	2012	2013	2014
RUR, billion	8.34	9.17	10.34	10.57	9.84	8.47
Growth Year on Year, %		9.9	12.8	2.2	-7.1	-13.9
US Dollars, million	262.93	300.85	352.30	340.10	308.34	215.3
Average annual exchange rate	31.72	30.48	29.35	31.07	31.9	39.34

Source: Rosinter data

RP-Com (Restaurant Professional Company) is one of the top 20 foodservice operators in Moscow. RP-Com currently owns the following restaurants in Moscow: twelve Goodman steakhouses (also with branches in Novosibirsk, London, Zurich and Kiev), two Filimonova & Yankel fish-houses, six Kolbasoff beer-restaurants. During its ten years of foodservice experience, the company has gained success in the niche steak house restaurants. This type of restaurant is less developed in Russia, and

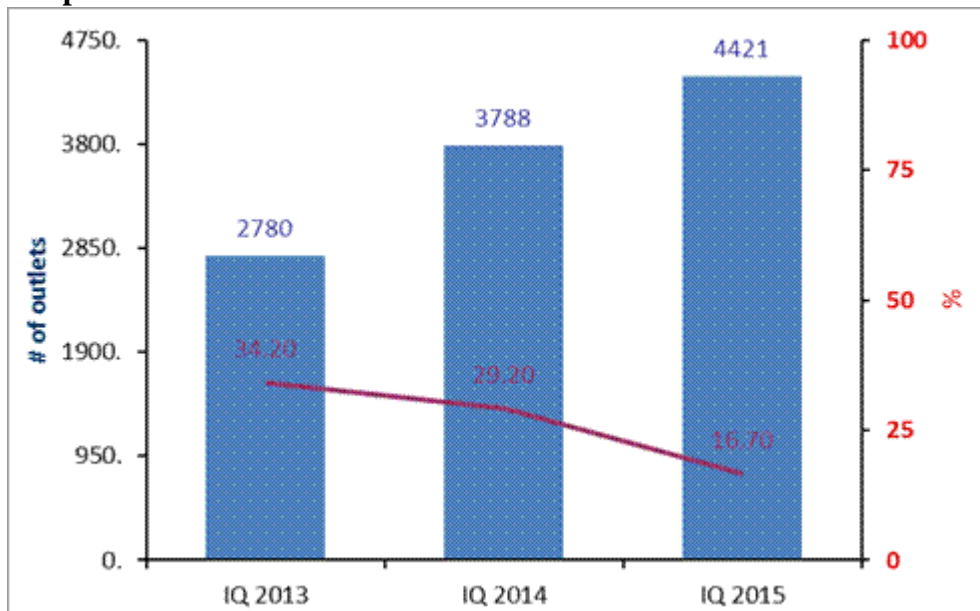
currently only a few independent operators specialize in grill menus. The Goodman chain became the largest chain of North American full-service restaurants in Moscow as well as in the whole of Russia.

Fast Food

According to Euromonitor International, fast food value sales increased by 16 percent and reached 407 billion rubles in 2014. Fast food remained one of the main foodservice drivers and even during complicated situation of 2014-2015 international and Russian operators managed to expand through Russia thank to franchise partnership model. Without a doubt, franchising is one of the main tools of fast food business development, especially in the chained segment. Chained fast food dominates in chained consumer foodservice with 57 percent of chained outlets in 2014.

Chained fast food value sales in 2014 exceeded independent operators' sales, generating 53 percent of total value sales and reaching 216.7 billion rubles. This reflects Russian customers' preference for well-known and stable foodservice standards provided by the chained segment – a fact which is confirmed by outlet growth. Today fast food is the most popular segment for young and middle-aged Russian consumers. Research has shown that more than 54 percent of fast food restaurants visitors are from 18 to 34 years old with average monthly income of 30,000 rubles.

Graph 6. Russia: Number of Fast Food Chained Restaurants in Russia in 2013-2015



Source: RBC research

While the economic slowdown and currency devaluation are slowing down fast food expansion in Russia, research of Russian Franchise Association has shown that today foodservice market sees some shift of customers from expensive restaurant formats to casual places with affordable prices. Currently about 70 percent of the residents of major Russian cities several times a month have visiting fast-food outlets with average checks of 150-300 Rubles on a regular basis. Pancakes, burgers, sandwiches, chicken, pizza, and baked potatoes are the most popular types of fast-food in Russia.

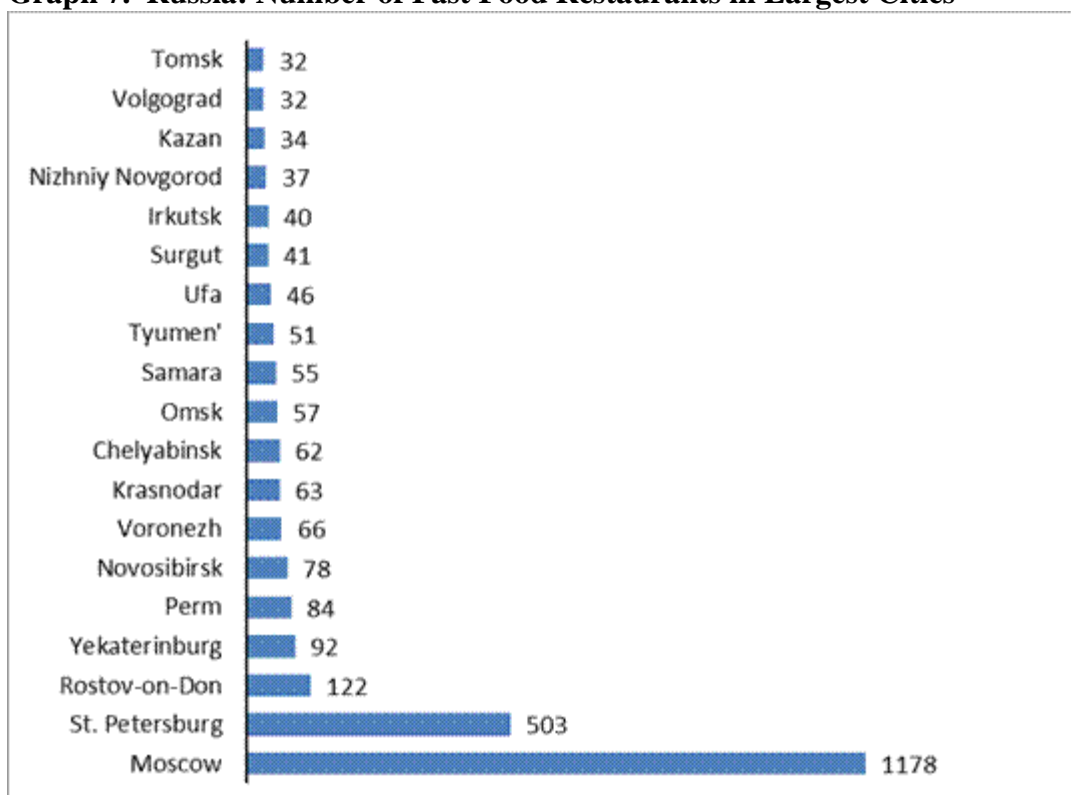
Table 9. Russia: Fast Food Formats in Russia

Type	Leading Brands
Burger and sandwich	Subway, McDonald's, Burger King, Carl's Jr., Stardog!s
Chicken	KFC, Southern Fried Chicken
Ice cream	33 Penguins, Baskin Robbins, Tutti Fruitti Frozen Yougurt
Pizza	Sbarro, Papa John's, Pizza Hut, Domino's Pizza, Tashir pizza
Potato	Kroshka-Kartoshka
Bliny	Teremok, Chaynaya lozhka
Bakery	Cinnabon, Dunkin' Donuts, Wetzels Pretzels, Krispy Kreme, Magnolia Bakery, Auntie Anne's

Source: Fast food market research

Fast-food restaurant chains tend to use a higher percentage of local ingredients (around 70-85 percent) as compared to other restaurants and charge much less. Several fast-food chains have created internal supply-chains based in Russia in recent years. For example McDonald's, which operates roughly 520 restaurants throughout the country, gets 85 percent of its menu items from domestic suppliers. At the moment, famous multinational chains are mostly represented in the largest Russian cities, Moscow and St Petersburg, where they have 29 percent and 21 percent outlet shares respectively. However, it is notable from year to year global fast food chains are expanding to other regions, where independent operators have the leading positions.

Graph 7. Russia: Number of Fast Food Restaurants in Largest Cities



Source: RBC research, May 2014

International franchises doing business in Russia include Burger King, Subway, Baskin-Robbins, Dunkin' Donuts, and KFC with the franchise system are most prevalent in Moscow and St. Petersburg. The most dynamic chains -- including KFC Burger King, Kroshka-Kartoshka, and Baskin-Robbins -- have opened numerous outlets in shopping malls and hypermarkets. Franchising is a key expansion method for transnational foodservice chains in Russia. According to expert estimates share of foreign brands on Russian restaurant market is about 40 percent. American fast food formats dominate in Russia and have fastest growth; among them are Subway, McDonald's, KFC, Burger King, and Baskin Robbins.

Table 10. Russia: Growth of Fast Food Restaurant Chains in Russia, 10 leading chains

Chain name	Country of origin	Year est. in Russia	# outlets July, 2014	# outlets July, 2015	change # outlets
Stardog!s*	Russia	1993	905	828	-77
Subway	USA	1994	691	670	-21
33 Penguins	Russia	2004	419	521	102
McDonald's	USA (Canada)	1990	433	517	84
Kroshka-Kartoshka	Russia	1998	368	388	20
Baskin Robbins	USA	1992	300	327	27
KFC	USA	1993	268	358	90
Teremok	Russia	1998	247	230	-17
Burger King	USA	2010	228	290	62
Sbarro	USA	1998	147	150	3

Source: Foodservice magazine, trade press, companies' web-sites

*street-food kiosks

Impressive dynamics is demonstrated by Tomsk chain of ice cream cafes 33 Penguins with 521 outlets, it opened 102 new cafes from July 2014 - July 2015. The Russian ice cream fast food chain 33 Penguins is seeing rapid growth based on its low start-up and operating costs (the only equipment needed is a refrigerator). Outlets are primarily located in retail locations and serve a quick, low-priced demand.

As of July 2015, leader of fast food restaurants **Subway** had 670 outlets in all Russian regions, including the Far Eastern Federal District. In 2011, Subway managed to outrun McDonald's in terms of outlets in Russia. In 2014 Subway reduced lump sum from \$ 12 thousand to \$ 7.5 thousand to support franchisees during the crisis and thus of course increased trust and interest to this brand.

Former leader in terms of quantity of chain eating places **McDonald's** is the leader of Russian fast food market in value terms. McDonald's entered Russia in 1990 and opened its first restaurant in the center of Moscow. As of December, 2015 McDonald's had 523 restaurants in 85 Russian cities, including McCafes, operating throughout Russia and serving about 1 million customers daily. On McDonald's 25th anniversary in Russia in January 2015, company reported serving 3 billion customers. Until April 2012, McDonald's had been expanding in Russia through self-operated stores only. McDonald's gave Rosinter Restaurant holding the subsidiary right to develop the chain in railway stations and airports in Moscow and St. Petersburg. So far only two McDonald's outlet was opened by Rosinter in St.

Petersburg airport Pulkovo. McDonald's sales in Russia totaled \$2.2 billion (641.4 billion rubles) in 2013 or about 8 percent of its worldwide sales of \$28.1 billion.

In August 2014 Federal Service for Supervision of Consumer Rights Protection and Human Welfare (Rosпотребнадзор) launched a campaign of sanitary checks at various McDonald's premises throughout the country. As a result, 3 McDonald's restaurants were closed in Moscow and about 10 in regions, though all of them eventually reopened. Despite the claims made by Russia's consumer watchdog, McDonald's opened 53 new outlets in 2015, although number of new outlets decreased compared to 2014, when 73 restaurants were opened. In August 2015 fast food giant signed a big franchise contract with "GiD" LLC which implies start of about 20 new "McDonald's" outlets in Novosibirsk, Tomsk, Omsk, Barnaul, Novokuznetsk and Kemerovo.

Baskin Robbins is somehow lagging behind the leaders with 327 chain eating places under this brand. Baskin Robbins, the world's largest chain of ice cream specialty shops, entered Russia in 1990. In 1996, the company opened a major ice cream plant in Moscow -- the biggest in Europe -- able to churn out 16,500 metric tons annually. The company sells more than 140 flavors of premium ice cream. The largest Baskin Robbins ice cream cafe in Europe opened in Moscow's Novyy Arbat in July 2011. Franchise stimulating measure, such as lump sum reduction has taken by Baskin-Robbins since autumn 2014.

Despite stunning dynamics of recent 2-3 years Russian market of fast food chains still has good growth potential. Stand-alone kiosks are popular in Russia, but there is some consolidation in the industry. The number of independent stands is decreasing, but sales and the number of chained outlets are increasing. Domestic chains dominate the street fast-food market. Chains such as **Stardog's** (hot dogs), **Krosha-Kartoshka** (potato stand), and **Teremok** (Russian crepes) are located throughout the major cities and are expanding regionally as well. Thank to developed franchise schemes transnational chains start to gradually push Russian restaurant projects off the market. This first of all refers to chains Teremok and Kroshka-Kartoshka. Despite distinct target on Russian consumer, well-thought menu with respect to national traditions and preferences (traditional Russian meals - pancakes/crepes and baked potato) these chains have lost their shares of market pie to global players every year.

Burger King has established a presence in Russia by opening its first restaurant in Moscow on January, 2010. Burger King is using its traditional franchising scheme to expand the chain in Russia. In order to launch operations in Russia, Burger King has established a daughter company Burger Rus, managed by Alexander Kolobov who has also successfully established a well-known coffee -shop chain called Shokoladnitsa. Under the terms of its franchise agreement, Shokoladnitsa is required to give 5 percent of its turnover to Burger King while Burger King is required to pay for the opening of each restaurant. In June 2012, Burger King and the Russian franchisee Burger Rus established a joint venture with VTB Capital, the investment arm of Russia's second biggest lender, to develop and expand the restaurant's chain and brand presence in the country. Thanks to that partnership Burger King opened 62 new restaurants in Russia from July 2014 to July 2015, expanding its chain to 290 and opening the outlets all over the Russia.

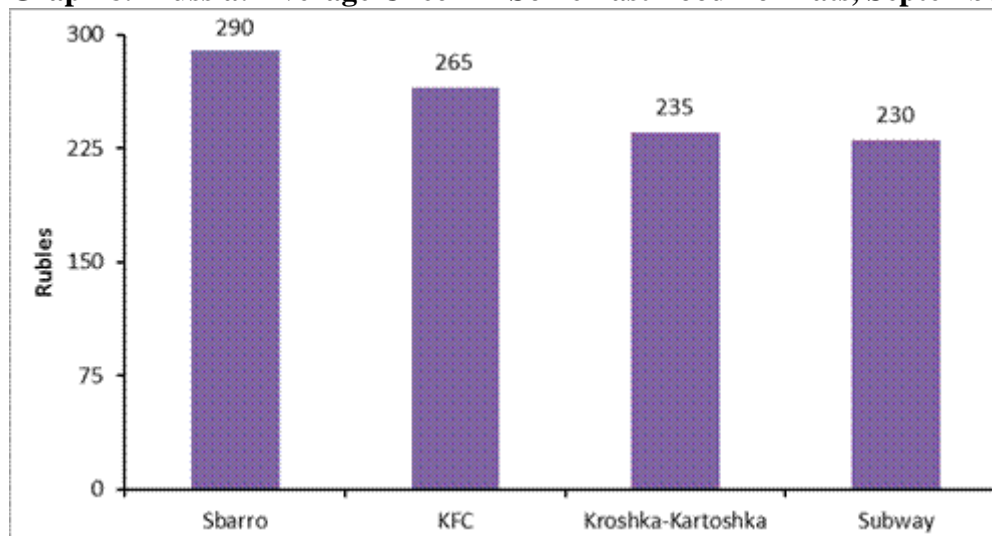
Russia has had the highest **KFC** store sales growth out of our 20 business units around the world. As of July, 2015 in Russia operate 358 KFC restaurants. According to surveys, the typical KFC customer is between 16 to 39 years of age, is not afraid to try new things and wants to see society progress while

enjoying a Western dining experience. The average check at local KFCs amounts to 265 rubles per person. Holding " G.M.P. Hospitality Planet" (brands Sbarro, Yolki-Palki, Yam Kee) has cut the size of regular payments, royalties, from 7 to 5 percent. Additionally holding company has expanded the range of services for companies intended to open a new foodservice outlets. Franchisor has taken over development and design of spaces, has chosen suppliers and signs contracts with them. Last year the revenue of KFC in Russia has increased by 40 percent compared to 2013. Sales revenue of the KFC fast food restaurants in Russia in the third quarter of 2015 grew by 45 percent.

2014 is one of the key years for development **Sbarro** in Russia, because the company launched the project of assortment standardization. Currently, the company operates 150 pizza restaurants.

When choosing a fast food place 54 percent of Russians prefer McDonald's, which speaks for high customer loyalty.

Graph 8. Russia: Average Check in Some Fast Food Formats, September 2014



Source: Foodservice magazine of September 2014

According to RBC research, the average check at fast food restaurants virtually unchanged last four years. On average, when visiting fast food establishments, Russians spend about 253 rubles. Food ingredients substitution is not so critical for fast food, because restaurants tend to use a higher percentage of local ingredients (around 70-85 percent) as compared to other restaurants. This decision is driven by high turnover and the need for a consistent supply-chain more than by direct preference.

Several fast-food chains have created internal supply-chains based in Russia. For example, McDonald's gets 85 percent of its menu items from 160 domestic suppliers. Burger King restaurants in Russia get a significant share of their food from domestic suppliers. The company has about 40 suppliers in Russia, of which more than half are local producers. Since 2010 Marr Russia supplies frozen hamburgers to McDonald's, KFC, and Burger King outlets. KFC works only with domestic suppliers. Last year Subway found substitution of imported cheeses and now works only with local ingredients as well.

Table 11. Russia: Other USA Fast Food Restaurant Chains in Russia, 2015

Chain name	Country of origin	Year est. in Russia	# outlets
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Cinnabon	USA	2009	107
Papa John's	USA	2010	68
Dunkin Donuts	USA	1996/2010	29
Krispy Kreme	USA	September, 2013	15
Carl's Junior	USA	2007	14
Wetzel's Pretzels	USA	December, 2013	8
Nathan's Famous	USA	September, 2013	12

Source: Trade press, companies' web-sites

The major ingredient for pizza fast food format is cheese, so Pizza Hut, Domino's Pizza and Papa John's chains are trying to substitute cheese from banned countries to local product. The Russian franchise operator of Papa John's, which has 68 outlets in the Russia, froze expansion plans due to the high inflation from the food import ban.

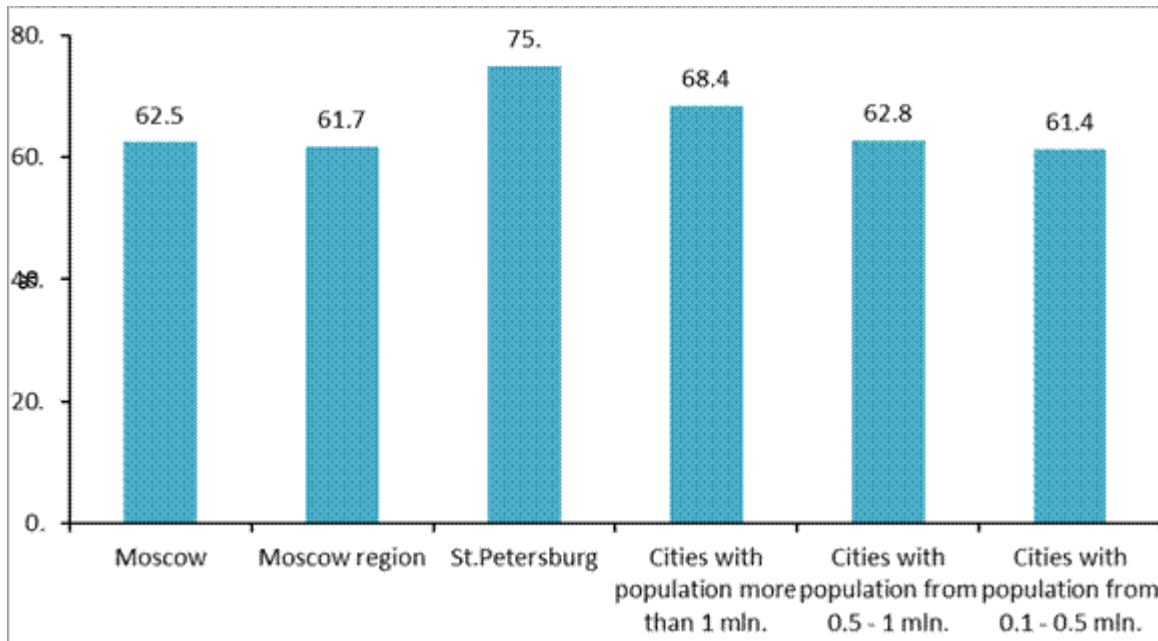
Taking into account the macroeconomic difficulties and the financial crisis, the emergence of new major players in the country is not expected. In some cases, franchisors are ready to end the relationship with franchisees, if they are not assured in the development strategy of Russian business partner. In January 2015, American franchisor CKE Restaurant did not extend general licenses for Russian company Yarkaya Zvezda, which was the master franchisee and operator of Carl's Jr. restaurants in Russia and had worked in the country since 2006. The master franchise owner pointed also another reason – it was impossible further development of chain due to high currency rates, increase the purchase price of products and erosion of purchasing power. As a result, California-based fast-food chain Carl's Jr. closed 26 restaurants in St. Petersburg, four in Novosibirsk and one in Krasnodar amid a volatile economic environment. Eight Wendy's restaurants were shut down in summer 2014 in Russia, because restaurant holding RPSCom, which developed American chain in Russia, changed the owner.

Coffeehouses

The popularity of cafés among urban consumers in the largest Russian cities is large and growing. Currently there are roughly 5,300 cafés in Russia. About 1,340 of them are managed by 80 chain operators. According to Euromonitor International, the sale of the specialist coffee shops reached 35.5 billion rubles in 2014 (9.9 percent increase in comparison to 2013). The number of outlets grows by 8.3 percent and reached 2715 units, riding a wave of interest in coffee culture, particularly among the urban affluent consumer. Most cafés are concentrated in Moscow – about 670, and in St. Petersburg - about 470 coffeehouses. Well-known multinational brands remain mainly represented in the biggest state cities, while major local companies continue their rapid expansion to the regions, developing their chains via franchising.

Market analysts have stated that 65 percent of residents from 18 to 54 years of age from cities with a population of more than 100 thousand visited cafés in 2014.

Graph 9. Russia: Visits to Cafes in Russian Cities, % of population



Source: RBC Research

There is an increasingly high concentration of the leading chains, including Shokoladnitsa, Coffeeshop Company, Starbucks, McCafe and Costa Coffee in these cities leading many of these chains to expand to the Russian regions. Non-chain cafés are significantly less common in the large cities. The rapid development of modern hypermarkets, trade centers, shopping malls, and business centers is helping leading chains, more so than independents, to enter regional markets.

Table 12. Russia: Market Share of Chained Café Leaders, in Percentage

Brand	Company name	2011	2012	2013	2014
Shokoladnitsa	Gallery Alex OOO	26	24.3	23.6	22
Coffee - House	Gallery Alex OOO	-	-	-	11.5
Coffeeshop Company	Schärf Coffeeshop GmbH	6.7	8.3	7.5	8.6
Starbucks	Starbucks Corp	5.3	4.9	4.1	5.3
McCafe	McDonald's Corp	2.0	1.6	1.4	1.4
Costa Coffee	Whitbread Plc	2.2	1.6	1.1	0.8
Traveler's Coffee	Traveler's Coffee OOO	1.3	1.3	1.2	1.3
Others		56.5	58	61.1	49.1
Total		100	100	100	100

Source: Euromonitor International

In 2014, Gallery Alex (owner of Shokoladnitsa coffeehouse chain), became coffee house market monopolist, as it bought the Coffee House brand from its main competitor, Coffee House Espresso & Cappuccino Bar. Therefore, from 6 October 2014, Gallery Alex operated 646 outlets in total throughout Russia, and accounted for a 13 percent value sales share within cafés/bars. The successful deal resulted in the company's value sales increasing by 61 percent to reach 12.4 billion rubles in 2014. Thus, the company has managed to break away from its main multinational competitors such as Coffeeshop Company, Starbucks and Traveler's Coffee, which operated 262 outlets combined in 2014. However,

the Coffee House brand name is continued to exist for a while, and just a few chained outlets have been renamed so far. Despite the strong consolidation of its position, the company continues to attract customers with new menu offerings and promotions, developing its advertising and loyalty programs. Difficulties in the economy, imposed embargoes and the cost of its acquisition have forced the company to raise its prices.

Regions are now becoming the main focus in expansion plans as Moscow and St. Petersburg are near the saturation levels of other major European cities in terms of chained cafés and independent cafés presence. Franchising is one of the main tools of coffee shops development, especially in the chained segment. The leading Russian café chain **Shokoladnitsa** has already opened outlets not only in Moscow (where there are around 393 establishments under the brand) and St. Petersburg, but also in Yekaterinburg, Volgograd, Kazan, Kemerovo, Novosibirsk, Sochi, Rostov-on-Don, Ufa, Tyumen and Chita, as well as abroad: in Yerevan, in Almaty and in three cities of Ukraine. Moreover, at the moment it focuses on regional expansion to the far eastern region of Russia. Shokoladnitsa brand chained outlets are franchised across Russia and have a strong brand identity with Russian consumers. Shokoladnitsa is closer to an Italian type café with a cozy interior while Coffee House is a more American-style coffee shop, with the décor being airy and uncomplicated. As a result, the clientele differs: Coffee House is preferred by consumers under 30 while Shokoladnitsa is favored by a more mature audience. Most of the Coffee House and Shokoladnitsa outlets are located in the food courts of new shopping malls and business centers. Prior to the acquisition of Coffee House by Shokoladnitsa, Coffee House was investing heavily in chain development and incurring large debts.

In 1997 Christopher Tara Browne, a former music producer from America, opened in Siberia a café called **Traveler's Coffee**, which began as a small counter inside of a pizza shop. Due to the popularity of its offerings, Traveler's Coffee has expanded substantially. Currently the Traveler's Coffee brand name is used in 84 cafés by franchises in different Russian cities including Moscow and St. Petersburg. The shop even has its own roaster in Novosibirsk, setting it apart from many coffee shops, by giving it a higher degree of customization and roast control.

Foreign coffee chains and other western franchises face an increasingly difficult operating environment for their brands and the franchise businesses of local players. In 2007, two leading multinational coffee shop chains appeared on the Russian market, adopting different development strategies. The world leader, **Starbucks** Coffee Company, opened its first outlet in Moscow in September 2007. In December 2012, Starbucks finally opened its first café in St. Petersburg and currently operates 99 coffee shops in Russia, 75 of which are in the capital. The company is expanding Starbucks' Russian footprint beyond major cosmopolitan centers. In October 2014, **Costa Coffee** (Whitbread Plc) chain in Russia - through local franchise partner Rosinter Restaurants Holding - announced plans to aggressively expand beyond the Moscow market, but was able to open only one coffee house since that announcement.

Austrian chain **Coffeeshop Company** has operated in Russia since 2008 and currently is number two by coffee sales after Shokoladnitsa. Russia is among the company's largest export markets and is growing rapidly. The appearance of these leading multinational coffee chains in the Russian market has changed the position of the coffee shop segment. 85 coffee shops have been established in Russia with about half of them in St. Petersburg. In 2014, it bought 10 percent of the company "Coffee Set" working under the Austrian brand Coffeeshop Company and fixed rate for supply on 60 rubles per the euro for saving Russian franchisee business. The deal amounted to a 2 million euro investment which has used

to expand Coffeeshop Company cafés in Russia. As Russian franchisee reported, traffic and average check in the coffee shops reduced to 1.5 times in 2014. Coffeeshop Company closed few unprofitable outlets and have started to develop new format – coffee to go.

Table 13. Russia: Leading Coffeehouse Chains in Russia

Chain Name	First Year of Operation	# outlets July, 2014	# outlets July, 2015	% growth Year-on-Year
Shokoladnitsa	2001	403	512	27
Coffeeshop Company	2008	82	85	3.6
Traveler’s Coffee	1997	77	105	36.4
Starbucks	2007	75	99	32
Costa Coffee	2007	30	31	0.3

Source: Restaurateur magazine, Foodservice magazine, trade press

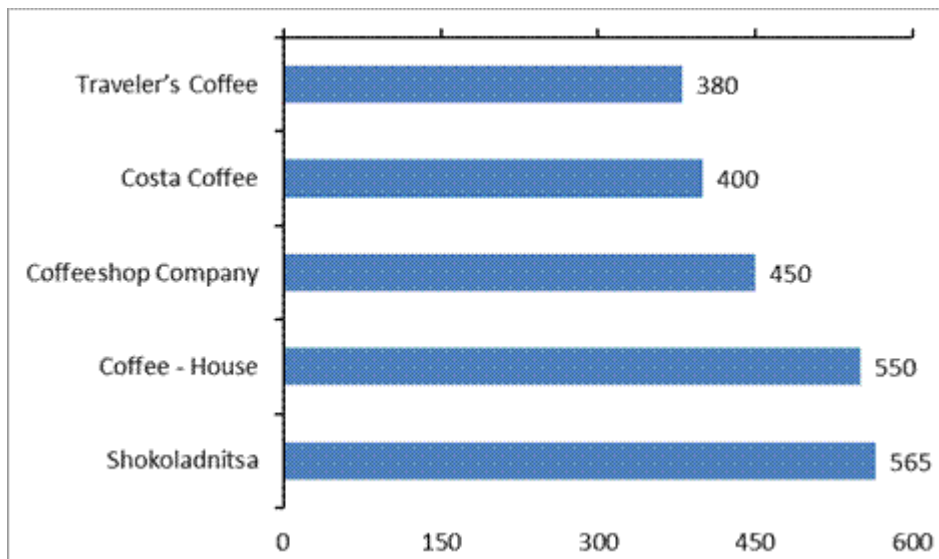
Table 14. Russia: Outlets of Leading Coffeehouses Chains, July 2015

Chain Name	Country of Origin	# outlets Corporate	# outlets Franchised	Websites
Shokoladnitsa	Russia	415	97	www.shoko.ru
Coffeeshop Company	Austria	43	42	www.coffeeshopcompany.ru
Traveler’s Coffee	Russia	21	84	www.travelerscoffee.ru
Starbucks	USA	99	-	www.starbucks.com
Costa Coffee	Great Britain	30	-	www.costa.co.uk

Source: Foodservice magazine, trade press

The typical Russian coffee shop format differs from western standards as Russian consumers prefer a larger assortment of drinks and food items. According to Foodservice magazine of 2014, drinks, including coffee, accounts for only 60 percent of sales at Coffee House, McCafe, Costa Coffee and Traveler’s Coffee; 43 percent for Shokoladnitsa, and 40 percent for Coffeeshop Company. Cafés in Russia constantly increase their non-coffee selections to include alcoholic drinks, dairy cocktails, salads, hot dishes, desserts, and tea. The average bill at café in Russia is between \$15 and \$25.

Graph 10. Russia: Average Check in Cafés, in Rubles



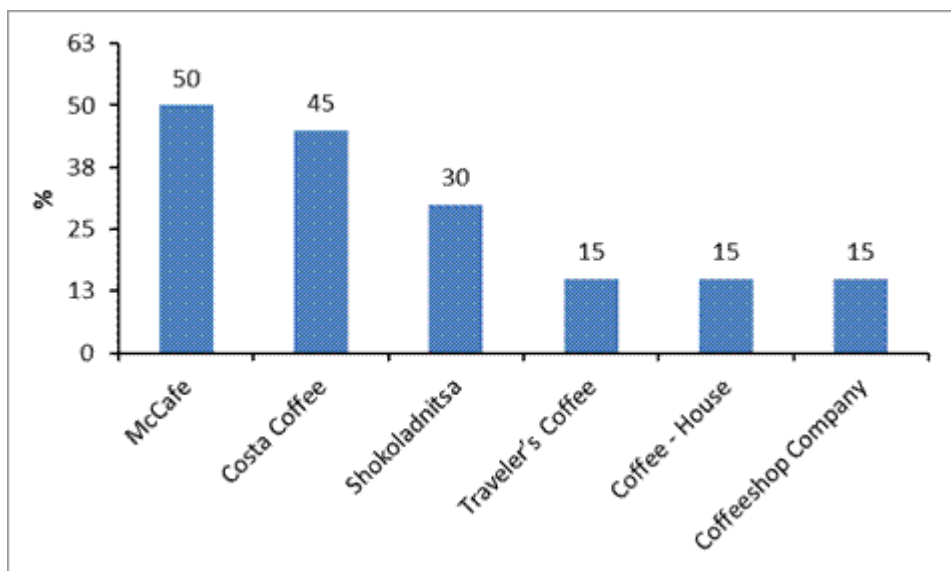
Source: Foodservice magazine of 2014

Russian coffee shops that sell a variety of desserts and confectionery products have created a new and interesting market for U.S. exporters of desserts, nuts, ingredients, and dried fruit. Traditionally, Russians have been large tea consumers going back several generations. But in the last decade, per capita coffee consumption has rapidly increased – by 4 times in 2012 compared to the level of 2000, when only 68 million people in the country regularly consumed coffee. In 2014, this figure, according to numerous forecasts, risen to 94 million people accounting for more than 60 percent of the Russian population. Leading market players are actively marketing coffee to the under 30 age group and increasing the numbers of cafés in Russia while at the same time facilitating a growing “to go” coffee culture.

Strengthening local brands are not the only problem for western coffee chains. As of September 2014, the Russian business confidence index remained near a one-year low as western sanctions on Russia further squeezed its struggling economy and consumer prospects. In addition to serious political tensions and economic hardship, chained coffee and independent cafes have also been forced to deal with a nationwide public smoking ban enacted in summer 2013. Smoking prevalence remains unusually high in Russia – 41.7 percent of the population in 2013 – and this could have a negative impact on coffee culture outside of the home.

Because of this policy change, take-away coffee transactions are a potential focus area for coffee chains in Russia although this requires changes in consumer behavior and preference. Currently all coffeehouses leaders are selling take-away coffee.

Graph 11. Russia: Share of Sales of “To Go” Coffee by Major Cafés, in Percentage



Source: Foodservice magazine of 2014

Hotel Sector SnapShot

The devaluation of the Russian ruble in 2015 has had a positive impact on hotels in Russia. Foreign visitors have benefited from the ruble depreciation and domestic travel has served as a main driver of growth in the industry. In the first three quarters of 2015, Russia experienced double-digit growth in hotel occupancy (+16.5 percent to 69.7 percent) and Revenue per Available Room (RevPAR) (+27.9 percent to 3,574.12 Russian rubles). Average Daily Rates (ADR) in the country was up 9.8 percent to 5,128.55 rubles. In addition, Sochi, a holiday destination, reported increases of 25 percent in occupancy and 40.9 percent in ADR. During the first nine months of 2015, 13 new hotels operating under international brands opened in Russia.

A difficult economic situation and an unfavorable exchange rate in Russia since autumn 2014 have brought in other types of tourists – domestic businessmen and wealthy Russian leisure travelers. The current geopolitical situation has led to a decrease in tourists from Europe, particularly from France, German, UK, and from the United States. At the same time, the tourist flow from Asia, with China on the first place, is gradually growing. The number of tourists from Finland has also increased, especially to the nearby city of Saint Petersburg.

Due to the devaluation of the ruble, travel to Russia becomes more affordable for foreign tourists. In 2014 -2015, the volume of outbound tourism also decreased due to the rising cost of traveling abroad, and Russians started to travel inside the country developing domestic tourism. These factors will have a positive effect on Russian hotel market in the next year. According to RosTourism, the results of 2014 showed a 40-percent increase in domestic tourism. The overall number of foreign tourists visiting Russia increased 16 percent in the first six months of 2015. Data from Russia's Federal State Statistics Service shows that the volume of the Russian hotel services market grew by 8.3 percent in 2014 to 175.7 billion rubles (\$4.5 billion), with average hotel occupancy at 50-60 percent in the regions and 70 percent in Moscow and St. Petersburg.

Table 15. Russia: Hotel Industry Sales, 2010-2014

	2010	2011	2012	2013	2014
Billion Rubles	112.8	125.5	141	162.3	175.7
Growth Year on Year, %		11.3	12.3	15.1	8.3
Average exchange rates by years	30.36	29.35	31.07	31.82	39.34
Number of hotels in Russia	7,866	8,406	9,316	9,869	10,714

Source: Federal State Statistics Service

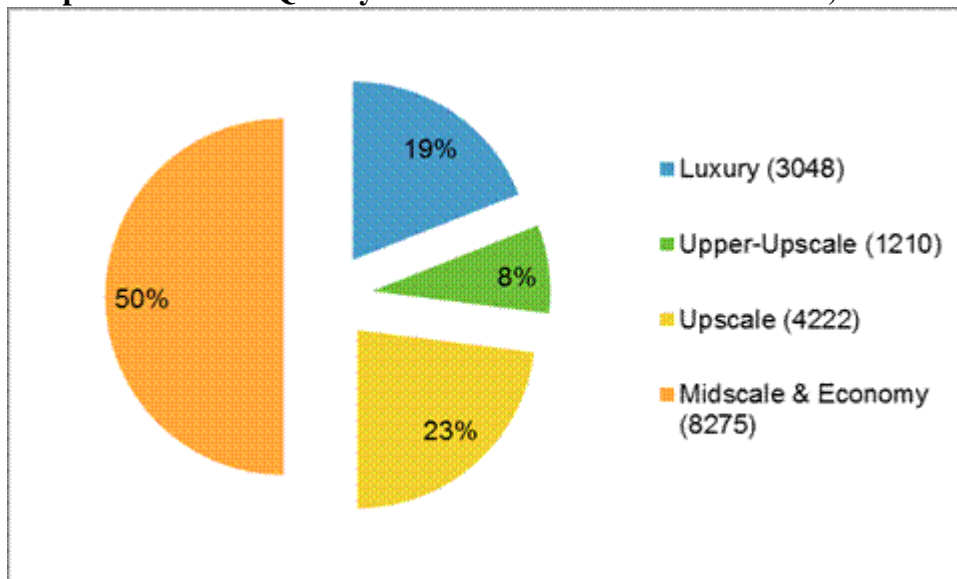
Moscow and St Petersburg alone account for around 25 percent of the country's hotel capacity. While the high-end sector is close to saturation, there is a strong demand for mid-level hotel rooms. The highest level of unfulfilled demand is for quality three star and economy hotels.

Moscow Hotel Market

268 hotels were operating in Moscow in March 2015. As recorded by Cushman & Wakefield Hospitality and Tourism department (C&W) in Q1 2015, Moscow quality room supply amounted to 15,600 units and its stock share is not more than 33 percent of the whole city's hotel market supply.

With the opening of 5 new hotels in 2015 of total rooms count to 1,117, distribution of quality supply by classes will be the following: 50 percent rooms will take Midscale and Economy hotels, 23 percent will comprise supply of Upscale segment hotels, 19 percent - Luxury hotels band 8 percent - hotels of Upper-Upscale segment. Thus, we see that Moscow hotel market is developing towards increase of Economy and Midscale supply.

Graph 12. Russia: Quality Moscow Hotel Market Structure, 2015



Source: Cushman & Wakefield Hospitality and Tourism

As the result of ruble devaluation in December 2014 - February 2015 the decrease of Moscow quality hotel average price in Q1 2015 amounted to 43 percent relative to Q1 2014 price - from \$172 per night to \$98. However, ruble prices had a slight growth in Q1 2015 - +2.4 percent in average to Q1 2014.

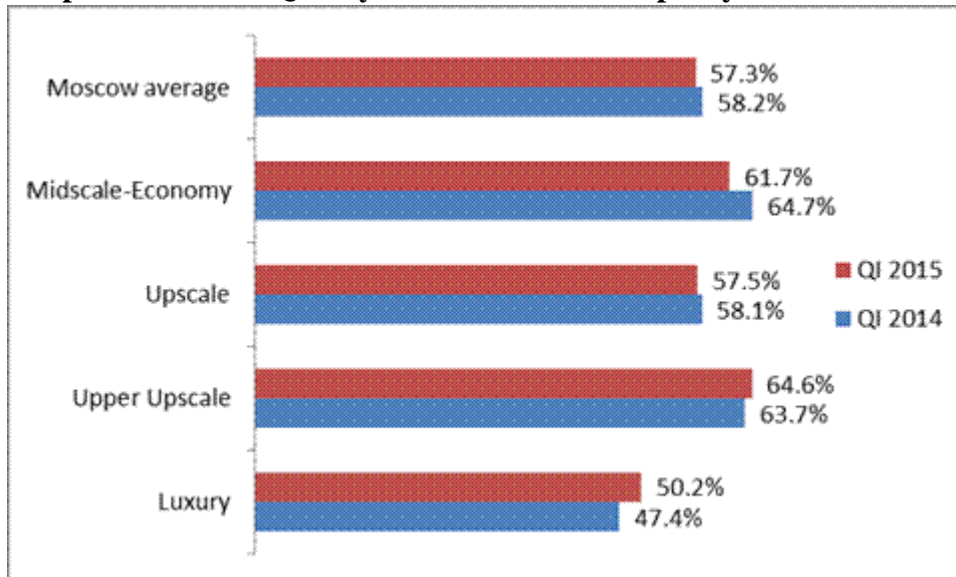
Table 16. Russia: Moscow Hotels Average Daily Rates (ADR)

	QI 2014 in USD	QI 2014 in Rubles	QI 2015 in USD	QI 2015 in Rubles
Luxury	329	11,496	191	11,950
Upper Upscale	233	8,160	124	7,781
Upscale	175	6,126	97	6,089
Midscale-Economy	129	4,505	73	4,566
Moscow average	172	6,012	98	6,153

Source: STR Global, Cushman & Wakefield Hospitality and Tourism

Slow recovery of hotel occupancy in Moscow, which emerged in December 2014, became more noticeable in Q1 2015.

Graph 13. Russia: Quality Moscow Hotel Occupancy



Source: STR Global, Cushman & Wakefield Hospitality and Tourism

Prices for accommodation in ruble equivalent has also started their growth in Q1 2015 as a consequence of compensation against significant inflation level reached 11.4 percent in 2014.

Table 17. Russia: Moscow Hotels Revenue per Available Room (RevPAR)

	QI 2014 in USD	QI 2014 in Rubles	QI 2015 in USD	QI 2015 in Rubles
Luxury	156	5,444	96	5,997
Upper Upscale	149	5,201	80	5,026
Upscale	102	3,562	56	3,499
Midscale-Economy	83	2,916	45	2,816
Moscow average	100	3,499	56	3,528

Source: STR Global, Cushman & Wakefield Hospitality and Tourism

This summer Moscow hosted much more tourists from Russia than usual. Due to the devaluation of the

ruble travel to Russia have become more affordable for foreign tourists. As a result the hotel market of the capital recorded extremely high operating performance growth in most segments. Moscow quality hotel occupancy reached 74 percent in summer of 2015. Moscow ADR was \$118.6 and RevPAR was \$85.4 in June-August of 2015.

According to Jones Lang LaSalle Inc., Moscow luxury hotels in September have registered the highest occupancy since 2007 (85 percent). Average daily rate of 14,732 rubles in this segment for nine months of 2015 has been at record high since 2008. This allowed for very solid revenue per available room gain of 18 percent compared to YTD number last year. Foreign visitors have benefited from the ruble depreciation and domestic travel has served as a main driver of growth in the industry.

Saint Petersburg Hotel Market

As of the end of 2014, the St. Petersburg hotel market had 139 hotels with approximately 19,800 rooms, excluding mini-hotels, and hostels. In September 2015 St. Petersburg has been named the best tourist destination in Europe by World Travel Awards. Statistics from the Federal Tourism Agency showed that the number of tourists visiting Russia’s Northern capital has increased by almost 60 percent in the first quarter of the year compared with the same period in 2014. Tourists from European countries, Turkey, China and India visited Russia’s cultural capital St Petersburg. About 23,500 Chinese tourists came to Russia in the first three months of this year, according to the Russian travel association “World Without Borders”.

According to Jones Lang LaSalle Inc., hotel occupancy for the first nine months of 2015 rose by 20 percent compared to last year, resulting in 7 out of 10 rooms being sold every night of the year so far. All segments except luxury attracted the unseen number of guests, registering occupancies of over 80 percent (and in some cases over 90 percent in the Upscale segment). Boosted by an 8 percent ADR gain in the same period (albeit mainly driven by the Luxury segment), across segments hotels were able to register a very solid increase in RevPAR of 28 percent or 900 rubles. Currently, seven hotels totaling over 1,200 rooms are under construction in St. Petersburg. This volume is expected for delivery by the end of 2016, unless the opening dates are not be postponed.

Table 18. Russia: St. Petersburg Hotels Scheduled for Opening in 2015-2016

	Name	# of Rooms	Class	Year Opening
1	Aston	160	4*	2015
2	Hilton	234	5*	2015
3	Hampton by Hilton	207	-	2015
4	Confidential	235	4*	2015
5	Holiday Inn	129	4*	2016
6	Jumeirah	74	5*	2016
7	Morskaya Stolitsa	200	3*	2016
Total:		1,239		

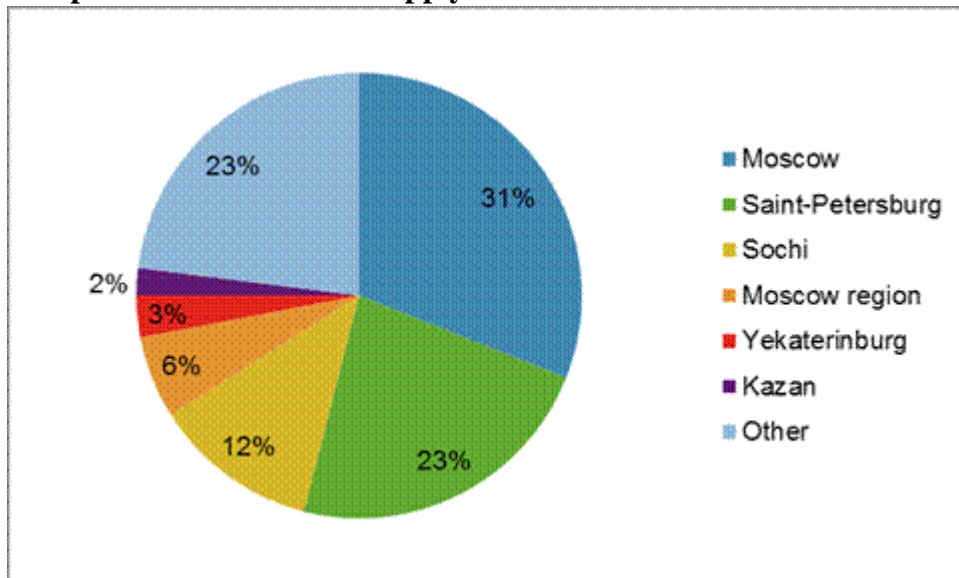
Source: STR Global

International Hotel Brands in Russia

According to the Ernst & Young (EY), in October 2015 there were 152 hotels under international

brands with the total room stock of 34,466 operating in 38 Russian cities and towns. More than a half of the existing rooms supply is concentrated in Moscow and St. Petersburg (54%), followed by Sochi (12%), the Moscow Region (6%), Ekaterinburg (3%) and other locations.

Graph 14. Russia: Room Supply with International Brands in Russian Regions, 2015



Source: Ernst & Young

Now 23 international hotel chains have operated or franchised in Russia. The largest International hotel chains are presented in the table below.

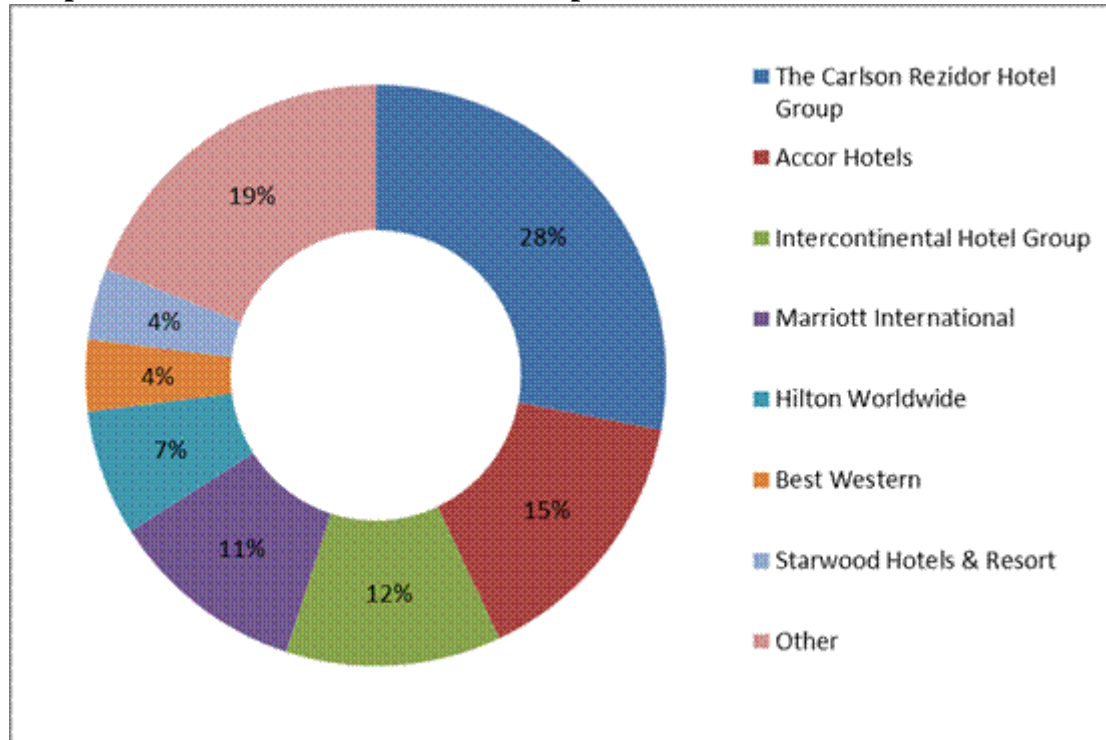
Table 19. Russia: International Hotel Operators, October 2015

Operator	Existing		Planned by 2020		Total by 2020	
	Hotels	Rooms	Hotels	Rooms	Hotels	Rooms
Accor Hotels	27	5,116	47	8,744	74	13,860
Hilton Worldwide	14	2,405	24	4,617	38	7,022
The Carlson Rezidor Hotel Group	34	9,524	4	886	38	10,410
InterContinental Hotels Group	16	4,164	12	3,276	28	7,440
Marriott International	16	3,844	8	1,732	24	5,576
Starwood Hotels & Resorts	7	1,434	8	1,651	15	3,085
Hyatt Hotels Corporation	3	700	5	1,218	8	1,918
Wyndham Hotel Group	3	446	5	760	8	1,206
Best Western	6	1,477	1	125	7	1,602
FRHI Hotels & Resorts	2	436	2	365	4	801
Other	24	4,920	2	76	26	4,996
Total:	152	34,466	118	23,450	270	57,916

Source: Hotel operator's data, Ernst & Young

The biggest market share - 66 percent - is divided between The Carlson Rezidor Hotel Group, Accor Hotels, InterContinental Hotels Group and Marriott International. During the first nine months of 2015 the Russian hotel market was supplemented by 13 new hotels operating under international brands.

Graph 15. Russia: International Hotel Operators Share in 2015



Source: Hotel operator's data, EY analysis

Russian Hotel Brands

In addition to international chains, Russian hotel operators increase their presence both in Russia and abroad. National hotel brands have a significantly smaller proportion of the market than those under international management. At the moment the share of the hotels under international brands (152 hotels) is almost 2.5 times higher than the share of the hotels under Russian management (73 hotels). The largest Russian hotel chains are presented in the table below.

Table 20. Russia: Hotel Operators in Regional and International Markets, October 2015

Hotel chain name	Number of hotels in Russia / abroad	Cities of presence in Russia	Countries of presence
Azimut Hotels	14 / 9	Moscow, St. Petersburg, Vladivostok, Murmansk, Ufa, Voronezh, Novosibirsk, Nizhny Novgorod, Kostroma, Astrakhan, Adler/Sochi	Germany, Austria
Amaks Hotels & Resorts	21 / 4	Perm, Vladimir, Kazan, Ufa, Belgorod, Rostov-on-Don, Tambov, Voronezh, Valday, Azov, Novgorod Veliky, Kurgan, Krasnoyarsk, Novy Urengoy, Staraya Russa, Yokshar-Ola, Tolyatti, Izhevsk, Omsk, Ust-Kachka, Essentuki	Belarus
Heliopark Hotels & Resorts	10 / 2	Moscow, Moscow region, Kaliningrad, Nebug, Penza, Sochi, Suzdal	Germany, Switzerland
Intourist Hotel Group	5 / 3	Moscow, Petrozavodsk, Lipetsk region, Gorno-Altaysk	The Czech Republic, Italy, Namibia
Cronwell Hotels & Resorts	10 / 3	St. Petersburg, Hanti-Mansiysk, Uray, Balabanovo	Greece
Korston Hotels	3 / -	Moscow, Kazan, Serpukhov	-
Alliance Hotel Management	4 / -	Moscow, Obninsk, Saransk, Abakan, Tuapse	-
Soyuz Marins Grupp	6 / -	Nizhny Novgorod, Sochi, Yalta, Ekaterinburg, Novosibirsk, Rostov-on-Don	-
Total:	73 / 21		

Source: hotel operators' data, EY analysis

There are usually two restaurants in four-star hotels and three restaurants in five-star hotels. According to industry sources, tourists often eat breakfast and dinner in their hotel, but they eat lunch in the city. In an attempt to attract more of the tourist industry, hotels are offering special catering services for different events. On average, room rentals account for 70 percent of hotel income, services account for 10 percent, and food and beverages account for 20 percent.

Luxury hotels represent the best opportunity for selling American products to hotels. Other sub-categories usually have very limited foodservice offerings. Hotel restaurants operate like other restaurants and purchase items through distributors. American meat, fish, wine, spirits, and fruit are some of the better prospects for this segment. It is planned that by 2020 the number of hotels under international management will increase by 118 new properties (23,450 rooms). Thus, if by 2020 all announced hotels open, the number of hotels under international management in Russia will amount to 270 hotels (57,916 rooms) located in 54 towns and cities.

Hotel projects usually have a four to five-year development cycle, so international hotel operators are building hotels before upcoming events in the Russian regional centers. The following events are planned for the near future: the Wushu FINA World Championships in Kazan on autumn 2017 and the 2018 FIFA World Cup. Matches are to be held in 11 cities, including Moscow, St. Petersburg, Kaliningrad, Kazan, Yaroslavl, Nizhny Novgorod, Samara, Saransk, Rostov-on-Don, Volgograd, and Sochi. 2017 Wushu World Championship competitions will be held in facilities built for 2013 Summer Universiade, also hosted by Kazan. 10,000 hotel beds, including hotels with western brands, are

available in Kazan now. Currently the World Cup 2018 host cities are represented by 106 branded hotels. It is planned that by 2018 the number of hotels will increase by 61 new properties (12,977 rooms).

Institutions

Institution/catering is a challenging segment for American producers. Before the 1990s, catering was a miniscule segment of the Russian hospitality market. Now, catering is a quickly evolving industry, with Moscow claiming 62 percent of the market and St. Petersburg at 22 percent.

Table 21. Russia: Catering Market in Moscow

	2012	2013	2014
Market volume, million rubles	2,112	2,365	2,502
Annual growth, %	10	12	5.9

Source: Catering Service Company

There are an estimated 700 catering companies operating in Russia, including 20 major ones. Each year, 15 new companies enter and 20 companies exit this intensely competitive industry. Russia’s leading caterers are Sodexho, Mega Foods, Parad Catering, Brizol, and Master Foods which have total market share of about 50 percent of catering services. Estimated value of the catering business in Russia is \$250 million. The Russian catering market consists of several segments, each of which has a different service audience, number of players, average bill per person, and profit, including lunch deliveries; corporate catering; and off-premise catering.

Urban dwellers have less time to prepare their own meals, so they often dine out or have lunch delivered to the office. Lunch deliveries are a strong component of the catering business. The estimated value of the lunch catering business in Moscow was \$140 million in 2013. There is room for development, however, as only 15 percent of Moscow’s office employees eat lunch prepared by qualified chefs.

Office cafeterias form another changing segment. Until recently, most cafeterias operated in the Soviet fashion, offering few choices and low quality. As incomes grew, the office cafeteria concept began transforming. Corporate catering firms manage stationary foodservice facilities, placing them in office buildings, business parks, shopping centers, administrative complexes, and industrial facilities. Their goal is to give people high quality meals in these institutions on a daily basis. The average bill in office cafeterias is \$4 to \$6. Newer cafeterias are beginning to use higher quality ingredients. They still prefer to buy whole, non-processed items, and they are very price sensitive. Like many restaurants, they monitor prices weekly and do not hesitate to change suppliers or menus if they encounter a better price.

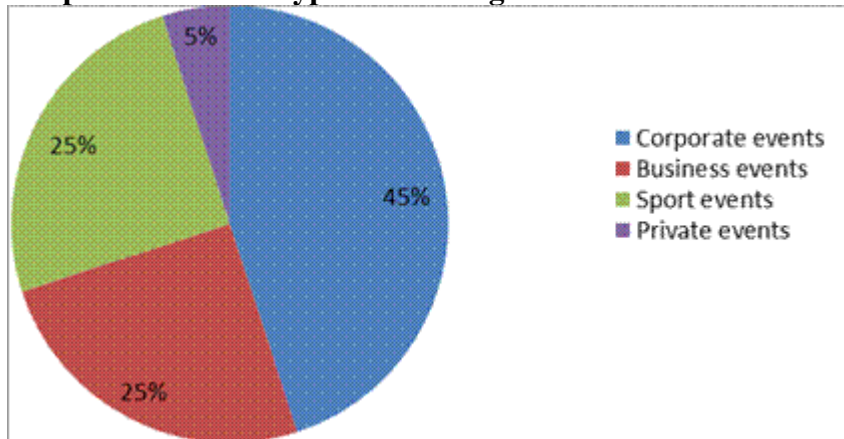
Catering for private events and parties, especially those in the premium segment is another attractive and profitable area of foodservice. Restaurateurs and five-star hotels are rushing to enter this lucrative market, including Gurme Catering, Baltshug Kempinski, and Swissôtel Krasnye Holmy. Their teams of culinary professionals are willing and able to delight customers. Hotels are attractive caterers because they are flexible enough to deliver a five-star experience in any venue, and they have an extensive wine knowledge. The average bill for mid-level off-premise catering is \$50 per person, but prices can be significantly higher in the premium class.

Table 22. Russia: Moscow Catering Segments

	Price, Rubles	Market Share
High-end segment	from 5500	25%
Mid-level segment	from 2500 to 5500	50%
Low-level segment	less than 2500	25%

Source: Catering Service Company

Graph 16. Russia: Type of Catering Events



Source: Catering Service Company

Caterers use many categories to tailor their products to the client, and they usually work with the same distributors as restaurants. Like restaurants, caterers use a variety of distributors and suppliers depending on their needs. Mid-level and high-end caterers import a variety of food, presenting an attractive opportunity for U.S. products. There is a particular demand for specialty items such as seafood, meat, wine, and nuts. Universities, schools, hospitals, and the military could be other potential customers for catering companies, but tenders are often not competitively bid for catering contracts with government institutions.

In 2008, Russian Railways created the joint venture Yedinaya Set Pitaniya with RP-Com, one of the top 20 foodservice operators in Moscow. This enterprise manufactures ready meals for passengers of the Russian high-speed railways, which currently operates on three lines: Moscow-St. Petersburg, Moscow-Nizhny Novgorod and St. Petersburg-Helsinki. By the end of 2010, the company produced 20,000 meal trays per day from its first catering facility near St. Petersburg. Other catering facilities have built in Yekaterinburg, Novosibirsk, Sochi, and Rostov-on-Don. According to RF Government plan, 8 Russian cities hosting 2018 World Cup matches should be linked by an integrated high-speed rail network.

Operators at the major airports in Moscow and St. Petersburg usually function more as part of a restaurant chain than as an institutional operator. According to airport statistics, 30 to 40 percent of passengers eat in airports. Leading Russian foodservice operator Rosinter has opened and operated restaurants in Russian airports since 2003. Its experience earned Rosinter the responsibility of being the primary foodservice operator in St. Petersburg's Pulkovo airport in 2007. In addition to operating the airport's restaurants, Rosinter also feeds the airport staff. Rosinter built a kitchen facility in the Pulkovo airport.

The volume of air passenger traffic in top 25 Russian airports exceeded 132 million in 2014 (10.2 percent increase). The volume of passenger traffic through Moscow’s airports, Domodedovo, Sheremetyevo, and Vnukovo, exceeded 77.3 million passengers in 2014 (9 percent increase). Airlines contract with professional catering companies for in-flight meals for passengers. JSC Domodedovo Air Service is the largest Russian company serving up to 60,000 in-flight meals and rations per day in Domodedovo airport. AeroMar has provided in-flight catering services to the passengers of Sheremetyevo airport since 1990.

Table 23. Russia: Largest Airports Passenger Traffic, in Million Persons

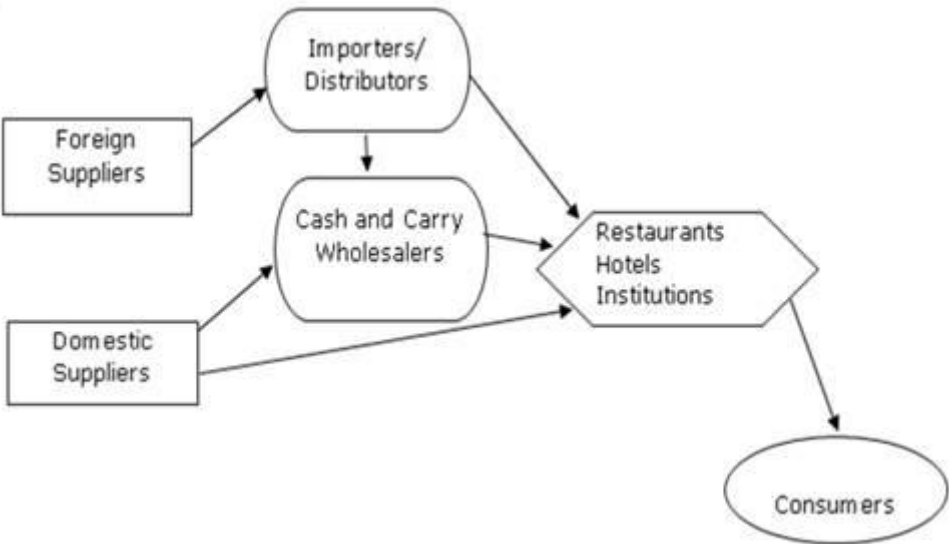
Airport	2013	2014	% Change 2014/2013
Domodedovo (Moscow)	30.76	33.04	7
Sheremetyevo (Moscow)	29.26	31.57	7.9
Pulkovo (St. Petersburg)	12.85	14.26	11
Vnukovo (Moscow)	11.18	12.73	13.9
Koltsovo (Yekaterinburg)	4.29	4.53	5.4
Tolmachevo (Novosibirsk)	3.75	3.96	5.6
Pashkovskiy (Krasnodar)	2.85	3.42	20
Adler (Sochi)	2.43	3.10	28

Source: Industry data

Joint-stock company "Rossiya Airlines" is the leading air carrier in North-West Russia. Rossiya Airlines is located in St. Petersburg and operates up to 40 percent flights from Pulkovo airport for more than 70 destinations. Since 1993, the airline has its own catering division. Daily, Rossiya Catering produces up to 20,000 portions of in-flight meals for all domestic and international airlines flying out from Pulkovo airport. Considering the increasing demand for high-quality airline food, airline foodservice could become an attractive niche market for U.S. food and beverage exporters.

SECTION II: ROAD MAP FOR MARKET ENTRY

Graph 17. Distribution Channels for HRI Products in the Russian Market



Domestic and imported food products for Russian foodservice establishments come through importers, distributors, and wholesalers. Large suppliers are typically also importers. For smaller restaurants and hotels, most foodservice purchases are made through a wholesaler or importer/distributor. Large chains may choose to purchase directly through customized growing agreements or through a central buying office. Most hotels and restaurants choose to purchase the majority of products through foodservice importers/distributors in the HRI sector, both large and small. Specialty and seasonal products are purchased through smaller distributors or directly from local producers.

Table 24. Russia: Advantages and Challenges for U.S. Exporters

Advantages	Challenges
Paying in Dollars is advantageous for exporting to Russia compared to Europe due to the lower cost of the Dollar relative to the Euro.	Ruble/\$ exchange rate has led to an increase in the price of U.S. products, mitigating some of the positive effects of the advantage over the Euro. Official government opposition to growth in food imports.
Russia’s 146 million people make it one of the largest consumer markets in Europe.	Economic crisis has had a profound impact on Russia and led to a decrease in purchasing power of many Russian consumers. Economic vulnerability, dependence on oil price.
Existence of large importers experienced in importing food products to Russia.	Complicated business environment due to the current food import ban affecting many U.S. products. An import substitution policy is being pushed by the Russian Government.
U.S. products have a reputation for consistency and high quality.	Logistics can be difficult. There are often long shipping times from the U.S., the major Russian port in St. Petersburg operates slowly and there can be complex customs regulations.
American-made food and drinks are still new for the majority of the population, and popular among the younger generation.	Growing number of domestically produced products; lack of knowledge of American products.
The HRI sector has a lot of room for growth. Restaurant chains are expanding out of Moscow and St. Petersburg to other cities with populations over one million.	Customers are very price sensitive. Food sanction has negative effect on trade.
Due to Russia’s 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.	Competition with food products imported from countries which are not in the banned list has risen.

Entry Strategy

Entering Russia’s market can be incredibly rewarding, but it requires hard work and careful planning by U.S. exporters. Different types of products require different marketing strategies. Many meat, seafood, wine, and spirits companies are selling U.S. products to the HRI sector and their businesses are flourishing. Several general recommendations may be helpful for developing a successful entry policy:

Work with a Russian Importer: Direct importation is difficult without a large customer base, so it is best to find an importer. To work with Russian Customs, it is essential to have a physical presence in Russia. U.S. exporters can approach the Russian HRI food and beverages market through a general importer, with whom good relations are essential. Selecting the right trading partner is one of the most important decisions for exporters when developing their businesses in Russia. A local Russian partner who is familiar with market conditions and the regulatory environment can help exporters navigate the Russian HRI market, resolve issues, and increase the likelihood of success. The importer should be able to handle customs clearance, veterinary and phytosanitary inspection requirements, any necessary guarantees, and all licensing procedures.

Logistics must be carefully considered and monitored, so close contact with the importer is also necessary in order to avoid logistical problems and shipping delays. Consider the longer shipping time for U.S. products compared to products from Europe. It is essential, for example, that all required documents be filled out as quickly and efficiently as possible. Most products will enter Russia through St. Petersburg, but if a U.S. exporter wishes to operate in the Russian Far East, Vladivostok is another option. Consistency and necessary quantities of production in the supply chain are frequently cited as primary concerns for the HRI segment.

Exporters representing U.S. companies may contact the Moscow ATO for assistance in locating importers. Performing due diligence is nevertheless important, and exporters are expected to verify the banking and supplier references of potential importers. Local and U.S.-based organizations in Russia can also provide helpful information to exporters. Credit reporting, however, is a relatively new practice in Russia, and credit-reporting agencies may not have complete information on potential Russian business partners. It is common for U.S. exporters to require 100% pre-payment for the first shipment.

Work with a Russian Distributor: U.S. exporters will need a distributor in order to sell their products. Large suppliers are typically also importers, and most HRI outlets rarely import products directly, preferring to procure supplies through local distributors. International chains with internal distribution networks within the country are the exception. The larger distributors are suited for commodity and large-volume sales. Smaller distributors work well for specialty, high-end, or new products that require marketing and product education. The most promising categories of products fall into this segment.

Provide Product Education: Marketing and product education are essential. Many of the HRI industry personnel are interested in new products, but they want to be shown how to use them and how the products can be made to work for them. Without some level of promotion, broader market penetration may be difficult. HRI sector players often mention “master classes” (chef trainings) and product demonstrations as useful for stimulating demand for new products. It is also important to determine the target audience and include both the distributor and the chefs in promotions. Technical support for U.S. producers in the form of printed material and/or seminars is critical to the effort to educate, dispel negative stereotypes, and ultimately build loyalty for U.S. products.

Attend Promotional Events: One of the main challenges for exporters entering the Russian market is product promotion. Participation in trade shows, technical demonstrations, and trade missions to the

United States are all marketing strategies that work well in the Russian market. A cost-effective way exporters can promote their products is to participate in World Food Moscow, the second largest and most professionally-run food and beverage trade show in Russia, held annually in September. Virtually all large food and beverage producers and importers participate in this show and USDA typically assists in organizing a U.S. pavilion. The ATO also recommends few interesting culinary-show opportunities in this area: PIR (Catering and Entertainment) Russia held each September/October in Moscow, ExpoHoReCa in St. Petersburg in early March, and the Vladivostok Culinary Festival, held each September. If exporters are targeting specific regions within Russia, the Moscow ATO recommends participating in regional exhibitions.

Participation in industry associations (US Meat Export Federation, California Wine Institute, etc., please refer to the list at the end of this report) that have a presence in Russia is also very beneficial.

Food Suppliers for the HRI Sector

Very few HRI businesses operate on exclusive contracts with vendors. Most chain and independent restaurants change suppliers frequently, particularly if there is a price difference. Most businesses use a separate supplier for each product category (i.e. produce, meat, or desserts) and very often work simultaneously with three to four suppliers of their principal ingredients to ensure steady supply. Whole foods are preferred and account for 70 percent of sales, principally because labor costs are low. Smaller restaurants without adequate space are usually the customers for semi-prepared items. Even fast-food chains tend to buy whole products and prepare them at the restaurant level. Exceptions to this include meat patties and French fries.

Few restaurants use fresh produce markets as suppliers. In contrast to U.S.-style produce markets, Russian markets have inconsistent supplies and offer goods of questionable quality. Markets also tend to have higher prices than other supply options. There are a large number of importers and distributors in the HRI sector, both large and small. A few work across a wide variety of products, but many specialize in a particular category. The distribution market is fragmented, and there are a variety of arrangements between suppliers and customers.

Metro Cash & Carry is one of Russia’s leading membership wholesale outlet chains. It has worked in Russia under the principles of small wholesaling since 2001. The company currently has 83 stores in 47 Russian regions, including twelve in Moscow and three in St. Petersburg. Foodservice operators across Russia have bought food, beverages, and other restaurant equipment from Metro Cash & Carry outlets. A reported Russian Metro Cash & Carry sale increased by 14.3 percent in 2014 and accounted 209.45 billion rubles.

Table 25. Russia: Major Suppliers of Food Products for Restaurants

Company	Principal Products	Customers	Locations
East-West www.ews.ru	Marbled Beef Veal Beef Pork Lamb Fish and Seafood	Restaurants Hotels	Moscow St. Petersburg Krasnodar Novosibirsk Yekaterinburg

	Poultry Groceries		
Global Foods www.globalfoods.ru	Marbled Beef Veal Beef Pork Lamb Poultry Fish and Seafood Groceries	Restaurants Hotels	Moscow St. Petersburg Krasnodar Yekaterinburg Vladimir Sochi Kazan Crimea other Russian regions
Australian Trade House www.austradehouse.ru	Marbled Beef Veal Beef Lamb Fish and Seafood Butter	Restaurants Supermarkets Hotels	Moscow
Marr Russia www.marr.ru	Marbled Beef Beef Veal Lamb Pork Poultry Fish and Seafood Groceries	Restaurants Supermarkets Hotels	Moscow St. Petersburg Rostov-on-Don Novosibirsk Samara
Miratorg www.miratorg.ru	Marbled Beef Veal Pork	Restaurants Supermarkets	Moscow St. Petersburg Regions
Snow World www.snowworld.ru	Veal Beef Pork Lamb Poultry Fish and Seafood Groceries	Restaurants Hotels	Moscow

Source: Industry data

Major suppliers of food products for the HRI sector have their offices in Moscow and St. Petersburg, Russia's primary restaurant markets. These offices handle foodservice-product imports and supply other Russian regions. The RFE and Siberia are highly dependent on imported foodservice products. Despite the tremendous distance between European Russia and the Russian Far East (RFE), 87 percent of the RFE's foodservice supply comes from Moscow and St. Petersburg. Several food products can reach Russia's Pacific Coast through the St. Petersburg port and still be price competitive. RFE and Siberian suppliers bring products to their regions from all over the world, using consolidated containers that have been imported and cleared in St. Petersburg or Moscow. High volumes enable large foodservice importers to gain better prices from global exporters.

SECTION III. COMPETITION

Russia imported approximately \$39.9 billion worth of agricultural products in 2014, according to Global Trade Atlas/Federal Customs Service. Year-on-year Russian agricultural imports can be seen in the following table:

Table 26. Russia: Growth in Agricultural Imports

	2010	2011	2012	2013	2014	Jan-Sept 2015
Agricultural Imports, billion dollars ¹	32.9	38.9	38.1	43.2	39.9	19.1
Growth Year-on-Year, %		18.2	-2.25	13.38	-7.75	
5-Year Average Annual Growth Rate, %					4.3	

¹ Total agricultural imports (includes HS codes 01 to 24).

Source: Global Trade Atlas/Federal Customs Service

Russia imported in value terms 7.75 percent less food products in 2014 compared to previous year, the Federal Customs Service reported. The food import ban was one of the main reasons for falling food imports in 2014 as well as shrinking consumer demand for imported products caused by the high exchange rate. Russia has significantly reduced imports of many types of agricultural commodities and food products. Imports of fresh vegetables rose 2.3 percent, dairy products – down 15.21 percent. Poultry meat import declined 5.62 percent, pork down 29.64 percent in 2014.

Table 27. Russia: Imports of Selected Foods from the World, in Million US Dollars

Product	HS Code	2012	2013	2014	% change 2014/2013	Jan-Sept. 2015	% change 3 quarters 2015/2014
Fresh & Chilled Beef	0201	218.55	424.4	472.67	11.37	259.86	-30.68
Frozen Beef	0202	2,583.31	2,457.26	2,249.48	-8.46	854.93	-45.33
Pork	0203	2,406.65	2,135.38	1,502.42	-29.64	680.18	-36.21
Poultry	0207	706.81	849.47	801.76	-5.62	277.16	-48.89
Lamb	0204	51.31	56.55	69.79	11.03	11.61	-74.33
Fish and Seafood	03	2,331.79	2,862.61	2,566.07	-10.36	978	-47.25
Dairy Products		2,037.16	4,192.74	3,555.15	-15.21	1307.98	-54.58
Fresh vegetables	07	2,433.57	2,892.66	2,959.08	2.3	1540.76	-38.08
Edible fruit and nuts	08	6,197.18	6,423.2	5,479.58	-14.69	2677.29	-34.71
Spirits	2208	1,399.60	1,484.15	1,237.25	-16.64	431.23	-47.55
Wine	2204	1,052.06	1,227.59	1,142.71	-6.91	468.56	-41.44

Source: Global Trade Atlas/Russian Federal Customs Service

In August 2014, Russia banned imports of a long list of beef, pork, poultry, fish, cheese, dairy products, fruits and vegetables from Australia, Canada, Norway, the United States and the European Union in response to the application of Western sanctions. To see the complete list of products affected by the ban, please refer to this [GAIN Report](#). On June 24, 2015, Russia extended the ban until August 5, 2016, and amended the list, removing some inputs needed by Russia’s fish farming sector while tightening the ban on dairy products (please see the [GAIN Report](#) for more detailed information). On August 13, 2015, Russia expanded the list of countries whose products were banned, adding the Republic of Albania, Montenegro, the Republic of Iceland, and the Principality of Liechtenstein. The ban will also apply to agricultural products from Ukraine no later than January 1, 2016, the date on which Ukraine is to implement a Free Trade Agreement with the EU. Russian President Vladimir Putin signed an order on November 28, 2015 establishing economic sanctions against Turkey over the downing of fighter jet that includes import restrictions on Turkish poultry, vegetables and fruits as of January 1, 2016.

Prior to the food import ban of August 2014, Russia was among the top export destinations for U.S. agricultural products. In calendar year 2013, the United States shipped \$ 1.3 billion of agricultural and related food products (including fish and forestry products) to Russia, and of this amount approximately 55 percent is attributable to products that are now restricted. Based on official Federal Customs Service data, the U.S. share of agricultural products includes (HS codes 01 to 24) exceeded \$1.36 billion in 2014 (drop 19.47 percent). The U.S. share of Russia’s agricultural imports in 2014 was 3.4 percent. In January-September of 2015 U.S. share of Russia’s agricultural products imports was \$409.7 million (down 63.75 percent compare to the first 9 months of 2014). The United States accounted for approximately 5 percent of Russia’s total agricultural imports in 2012; the market share declined to 2 percent in in the first 9 months of 2015.

As noted earlier, imported products account for a large percentage of ingredients used in the restaurant business. Russia’s largest suppliers (by sales) of all commodities to foodservice before August 2014 were Brazil, the United States, China, Turkey, the European Union, and CIS countries. No single country dominated the market but the largest share of products came from Europe.

After the ban Russia is changing geography of food suppliers. Russian importers currently work with Latin American countries, Israel, Morocco, Israel, Tunisia, Egypt, and South East Asia and fill agricultural product hole. New channels of import substitution often include higher logistics costs which affect the final price.

Table 28. Russia: New Geography of Food Suppliers for HRI Sector

Product	Previous Country Suppliers	Current Country Suppliers
Green salads	Netherlands, Italy, Israel	Israel, Russia
Dairy products	Poland, Lithuania, Finland	Russia, Belarus
Cheese	Italy, Spain, France, Lithuania, Germany	Russia, Belarus, Uruguay, Georgia
Vegetables	Poland, Netherlands, France, Greece, Italy, Spain	Turkey, Israel, Tunisia, Egypt, Russia
Fruits	Poland, Turkey, Greece, Spain	Russia, Turkey, Egypt
Beef	USA, Australia, Latin America, Germany	Latin America, Belarus, Russia
Salmon	Norway	Russia, Chili, Faroe Islands
Mediterranean	Greece, Turkey, France	Turkey, Tunisia, Morocco

fish		
Seafood	France, South East Asia, Norway, Turkey, New Zealand	Tunisia, Morocco, South East Asia, New Zealand
Meat gourmet	Spain, Italy	Belarus, Russia
Mushrooms	Poland, Netherlands	Russia

Source: Foodservice magazine, importers

This is extremely difficult situations for the fine dining and even mid-range restaurant which serves sushi, seafood and have European menus. There are no substitutions for some of the banned products, such as American lobsters, Italian parmesan, and French oysters. Companies, which work in fine dining segment and event catering, are mostly depended on imported food, so the product ban mostly affected restaurants belonging to the higher price category. While the HRI sector uses mostly imported products, some ingredients are purchased domestically. These include root vegetables, such as carrots and beets, and other basic vegetables like cabbage and potato. Currently HRI sector is trying to use local products as much as possible and find appropriate food product substitution.

Italy, France, and Spain are the major wine suppliers to Russia. Californian wines appeared in Russia nine years ago and sales are expanding but remain less than 2 percent of the total. The United Kingdom, France, and the United States supply popular spirits such as Bourbon, Tennessee and Scotch whiskey, cognac, rum, and brandy.

SECTION IV. BEST PRODUCT PROSPECTS

Interest in new product categories is growing. American products are consequently competitive and attractive to Russian importers. Currently importers are trying to find analogous to U.S. food products because of Russian food sanctions. Table 29 shows Russian imports of selected U.S. food products.

Table 29. Russia: Russian Imports of Selected Food from the U.S., millions of US Dollars

Product	2012	2013	2014	% change 2014/2013	% market share
Poultry	309.70	337.60	163.97	-51.43	20.45
Beef	236.95	0.69	0.37	-46.37	0.03
Pork	292.69	18.98	83.50	339.92	5.56
Tree Nuts	143.77	185.05	119.90	-35.20	35.24
Fish and Seafood	39.16	78.25	42.46	-45.74	1.49
Fresh Fruit	22.83	33.80	18.88	-44.14	0.38

Source: Global Trade Atlas/Russian Federal Customs Service

The U.S. is one of the world's leaders in developing the hospitality industry. U.S. producers can offer a wide range of products developed, manufactured, and packaged for the HRI sector. Several product categories are particularly attractive for export to Russia. Fresh and frozen seafood, frozen and chilled high-quality beef, pork, cheese, fruit and tree nuts are in demand.

Sauces, seasonings, and semi-prepared items have potential, but they require market education. Several industry experts discussed the need for low-fat goods, reduced-calorie dairy items, and bakery-preparation products.

Wines and spirits also have high potential, but there is a lack of awareness about American wines. Since 2013 American craft beer has appeared in Russia.

Table 30. Russia: Imports of Alcohol Beverages from the U.S., millions of US Dollars

Product	Calendar Years (Jan-Dec)			% change 2014/2013	% market share	Jan-Sept 2015	% change 3 quarters 2015/2014
	2012	2013	2014				
Spirits	69.16	94.96	88.89	-6.39	7.18	38.16	-37.75
Puerto Rico (U.S.) rum	34.93	43.62	38.18	-12.45	3.09	1.77	-89.85
Wine	12.34	15.68	13.81	-11.98	1.21	3.04	-70.58
Beer	0	0.06	0.26	326.35	0.13	0.41	66.71

Source: Federal Customs Service

Many distributors and importers work throughout Russia. For details on specific product segments, please contact the Agricultural Trade Office for a Buyers List.

SECTION V. POST CONTACT AND FURTHER INFORMATION

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

U.S. Agricultural Trade Office Headquarters, Moscow

Email: atomoscow@fas.usda.gov

Erik Hansen, Director

E-mail: Erik.Hansen@fas.usda.gov

Alla Putiy, Marketing Specialist

E-mail: Alla.Putiy@fas.usda.gov

Tatyana Kashtanova, Administrative Assistant

E-mail: Tatyana.Kashtanova@fas.usda.gov

Street address (for express parcels):

U.S. Agricultural Trade Office

American Embassy

Bolshoy Devyatinskiy pereulok, 8

121099, Moscow, Russia

Tel: 7 (495) 728-5560

Fax: 7 (495) 728-5069

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

Director, Agricultural Trade Office

5430 Moscow Place

Washington, DC 20521-5430

Covering Northwest Russia (St.Petersburg):

Svetlana Ilyina, ATO Marketing Specialist

American Consulate General

Furshtatskaya Street, 15

191028, St. Petersburg, Russia

Tel: 7 (812) 331-2880

Fax: 7 (812) 331-2675

E-mail: Svetlana.Ilyina@fas.usda.gov

Covering the Russian Far East (Vladivostok):

Oksana Lubentsova, ATO Marketing Specialist

American Consulate General

Pushkinskaya Street, 32

690001, Vladivostok, Russia

Tel: 7 (4232) 300-089

Fax: 7 (4232) 300-089

E-mail: LubentsovaOX@state.gov

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

FAS Website: 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

Office of Agricultural Affairs

American Embassy

(Address same as above for ATO Moscow)

Tel: 7 (495) 728-5222

Fax: 7 (495) 728-5133 or 728-5102

E-mail: agmoscow@fas.usda.gov

USDA Stakeholders

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.

Alaska Seafood Marketing Institute

Ksenia Gorovaya (St. Petersburg)

Address: 194223, St. Petersburg, Russia, Orbeli str., 25/3, office 7

Tel: 7 (921) 637-4199

E-mail: Ksenia@crispconsulting.ru

<http://crispconsulting.ru/>

Almond Board of California

RK Marketing Office,

29/1 Generala Tyuleneva Str., 117465, Moscow, Russia

Tel: 7 (495) 729-3080

Fax: 7 (495) 989-2670

E-mail: office@Almonds.ru

<http://www.Almonds.ru>

California Prune Board

Mark Dorman

Suite 18, Harborough Innovation Centre

Airfield Business Par, Leicester Road

Market Harborough, Leicestershire

LE16 7QX, UK

Tel: +44 (0) 1858 414218

Fax: +44 (0) 1858 469333

E-mail: info@cpbeurope.eu.com

Cranberry Marketing Committee

Ksenia Gorovaya (St. Petersburg)

Address: 194223, St. Petersburg, Russia, Orbeli str., 25/3, office 7

Tel.: 7 (921) 637-4199

E-mail: Ksenia@crispconsulting.ru

Web : www.uscranberries.com

Pear Bureau Northwest

Katerina Akulenko (Vladivostok)

Address: 690090 Vladivostok, Russia, Svetlanskaya str., 37, Office 2

Fax: 7 (4232) 63-8411

Tel.: 7 (4232) 56-5536

E-mail: katerina@newmark.ru

<http://www.usapears.ru>

Ksenia Gorovaya (St. Petersburg)

Address: 194223, St. Petersburg, Russia, Orbeli str., 25/3, office 7

Tel: +7 (921) 637-4199

E-mail: Ksenia@crispconsulting.ru

<http://crispconsulting.ru/>

US Apple Export Council

Ksenia Gorovaya

Address: 194223, St. Petersburg, Russia, Orbeli str., 25/3, office 7

Tel.: 7 (921) 637-4199

E-mail: Ksenia@crispconsulting.ru

USA Dry Pea and Lentil Council

Irina Koziy

Address: 117465, Moscow, Russia, Generala Tuleneva str., 29/1

Tel: 7 (495) 729-3080

Fax: 7 (495) 989-2670

Email: office@rkmarketing.ru

USA Poultry and Egg Export Council (USAPEEC)

Albert Davleev

Address: 123592, Moscow, Russia, Kulakova str., 20, Building 1A

Tel: 7 (495) 781-9200

Fax: 7 (495) 781-9201

E-mail: usapeec@usapeec.ru, albertdavleyev@yahoo.com

<http://www.usapeec.ru>

U.S. Meat Export Federation (USMEF)

Galina Kochubeyeva (Moscow)

Address: 119049, Moscow, Russia, Leninsky Prospekt, 2, 9th Floor, Business Center

Fax: 7 (495) 230-6849

Tel.: 7 (495) 544-9387

E-mail: moscow@usmef.org, gkochubeeva@usmef.org

Yuriy Barutkin (St. Petersburg)

Tel: 7 (911) 818-2610

E-mail: stpete@usmef.org

U.S. Wheat Associates

Valentina Shustova

Address: 129090, Moscow, Russia, Gilyarovskogo Str., 4, Stroyeniye 5, Office 101

Fax: 7 (495) 207-4203

Tel.: 7 (495) 956-9081; 7 (495) 208-8124

E-mail: uswmow@dol.ru

www.uswheat.ru

Washington Apple Commission

Ksenia Gorovaya (St. Petersburg)

Address: 194223, St. Petersburg, Russia, Orbeli str., 25/3, office 7

Tel: 7 (921) 637-4199
E-mail: Ksenia@crispconsulting.ru
www.bestapples.ru

Katerina Akulenko (Vladivostok)
Address: 690090, Vladivostok, Russia, Svetlanskaya str., 37, Office 2
Fax: 7 (4232) 63-8411
Tel.: 7 (4232) 56-5536
E-mail: katerina@newmark.ru

Wine Institute of California

Olga Tuzmukhamedova
Address: 127521, Moscow, Russia, Staromarinское shosse, 14-77
Tel: +7 926-389-5745
E-mail: 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

Address: 127006, Moscow, Russia, Dolgorukovskaya str., Building 7, 14th floor
Fax: 7 (495) 961-2142
Tel: 7 (495) 961-2141
Email: amchamru@amcham.ru
<http://amcham.ru/>

American Chamber of Commerce in St. Petersburg
Address: 190000, St. Petersburg, Russia, Yakubovicha str. 24, left wing, 3rd floor
Fax: 7 (812) 448-1645
Tel: 7 (812) 448-1646
Email: 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, HRI equipment, and packaging equipment or materials, refrigeration equipment, and other industrial products, please contact:

U.S. Commercial Service
Bolshoy Devyatinskiy pereulok, 8
121099 Moscow, Russia
Fax: 7 (495) 728-5585
Tel: 7 (495) 728-5580
E-mail: moscow.office.box@mail.doc.gov
<http://www.buyusa.gov/russia/en/>

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 with background and contact information for each potential partner. The U.S. Commercial Service has the capability to provide after-sales services such as customized market briefings and market research on the relevant industry sector.

The World Bank also maintain mission in Russia.

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>

[RS1215 Market Opportunities for Key U.S. Products in Russia](#)

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

[Food and Agricultural Import Regulations & Standards Country Report 2014](#)

[Dairy and Products Annual Report 2014](#)

[Demand Grows for US Distilled Spirits in Russia 2014](#)

[US Wine Export to Russia are on the Rise 2014](#)

[RS1554 Poultry and Products Annual](#)

[RSATO036 Retail Report / Annual](#)

[RFATO026 Exporter guide](#)

[RFATO025 Fresh Deciduous Fruit Annual](#)

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