

The Russian Food Sector

Still a Sector with Plenty of Opportunities!

19 June 2009

**Rusland Evenement ter gelegenheid van
het bezoek van President Medvedev, Amsterdam**

By: Jeroen Ketting, Managing Director of Lighthouse Russia BV

Contents of the Presentation:

1. Russia and the Crisis.
2. The Crisis and the Russian Food Sector.
3. Opportunities on the Russian Food Sector.
4. Conclusions and Questions.



A. Russia and the Crisis:

1. For years, the Russian food sector attracted foreign companies due to its rapid growth (**12% p.a.**), underdeveloped local production and increasing demand for Western food products.
2. Russia has been hit hard by the crisis:
 1. **GDP growth: 7% p.a. (1999-2008) → -7% (2009), 0% (2010).**
 2. **Consumer spending: 10% p.a. (1999-2008) → -4% (2009).**
 3. **Devaluation: Ruble vs \$/ € = -32% (Aug 2008 – June 2009).**
3. The effects of the crisis have created a **new reality** in the Russian food sector.
4. All players in the Russian food sector (consumers, retail, distributors and suppliers) are **adapting** to this new reality.



A. The Crisis and the Russian Food Sector: Consumers

1. **Consumer spending on food products:** Consumers are attempting to sustain their living standards of before the crisis by buying the same amount of products, but cheaper (esp. tea, coffee, cocoa, eggs, cheese, meat products and pasta) → Drop of **10-20%** in consumer spending on food products.
2. **Consumer preferences:**
 1. Demand for cheaper food products create an **opportunity** for **private label** products to develop as an alternative to the more expensive A brands. However, already positioned A brands will continue to hold a strong position as Russians are sensitive to A brands.
 2. **Local shops, open markets and discounters** have become more popular as they offer cheaper food products than supermarkets.
3. **Imports of food products: Drop** of 30% (Apr. 2009 vs. Apr 2008).

B. The Crisis and the Russian Food Sector: Retail Chains

1. Before the crisis: **Rapid expansion** of modern format retail chains: 12% (2002) → 33% (2008) of total food retail sales.
2. Retail chains were **heavily leveraged** to fund expansion → liquidity crisis:
 1. Cutting costs (e.g. closing outlets, reducing stocks and assortment).
 2. Slow down in expansion.
 3. Consolidation: Indebted chains forced out of the market or taken over.
3. Price **sensitive** due to decreased consumer spending → difficult to finance current assortment → assortment reduced by 15% and development of private labels as these are around 20% cheaper than A brands.
4. Retail chains are switching to **local fresh products** when in season. Metro started up distribution points in the regions where fruit and vegetables are collected, checked for quality, packed and distributed.

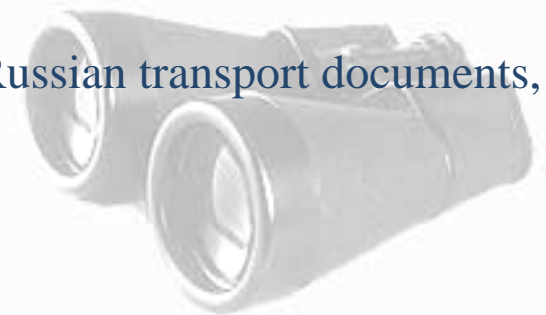
C. The Crisis and the Russian Food Sector: Retail Chains and Suppliers

Retailers are facing difficult times → demands on suppliers:

1. Be prepared to work **DDP** (Rubles) and with **longer payment terms** (90 days is an average payment term on the market – X5, 7th Continent).
2. Be prepared to make a **long-term investment** as success on the Russian market requires time, money and flexibility:
 1. **Time: Retail chains** are optimizing their assortment. Suppliers need to convince the chains that they offer better quality and / or price than an existing supplier (one in – one out). It takes time to convince them.
 2. **Money:** Offer competitive prices, BTL promotion and merchandising ideas in order to allow retailers to **attract sufficient customers**.
 3. **Flexibility:** Foreign companies should be **flexible**. Retailers expect their suppliers to be prepared to work closely together in optimizing logistics schemes, promotion campaigns and developing the assortment and type of packaging.

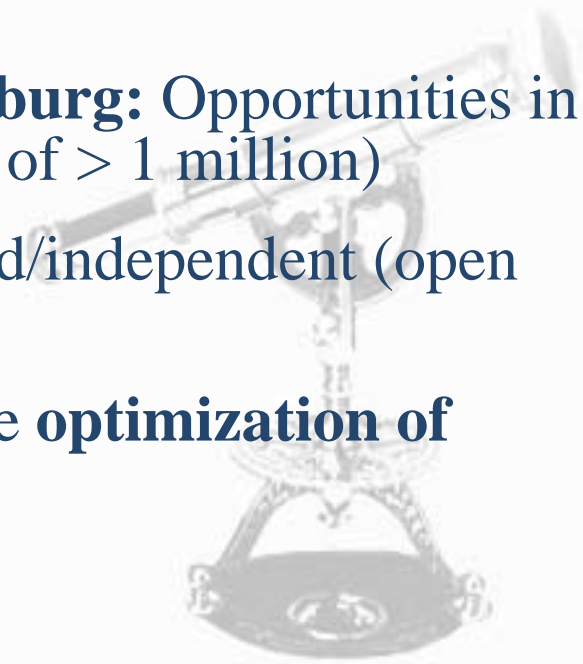
D. When you plan to enter the Russian market, keep in mind:

1. Price calculations.
2. Certification.
3. Logistics to Russia (and within Russia!).
4. Sales approach: Distributor? Own representative office?
5. Retail **conditions** (listing fees, marketing fees, logistic fees), e.g. listing fees EUR 100 per shop and per SKU, Perekrestok (X5 group) listing fees of up to EUR 100-200 k.
6. Russian buyers don't like to think → Approach Russian buyers with a **complete offer** (prices, assortment, pictures, budgets and timing).
7. Russian buyers are interested in **merchandising** and **BTL campaigns** financed by the supplier.
8. Internal: Is your organization ready for the Russian market? (Russian transport documents, invoices and so on are different to those in the Netherlands).
9. Manage your distributor: Frequent visits or local staff.
10. Specific Russian **business culture**.



Opportunities on the Russian Food Sector:

1. Population of 142 million will continue to consume → Food consumption will grow slowly in 2009/2010 (avg 6%) but is expected to rise from **\$230 bn.** in 2008 to **\$404 bn.** in 2013 > average annual growth of **12%!**
2. Local production is insufficient to meet local demand → **continued demand** for imports.
3. **Think further than Moscow and St. Petersburg:** Opportunities in the **regions** (11 other cities with a population of > 1 million)
4. Around **70%** of food retail is still unorganized/independent (open markets, pavilions, kiosks, grocery stores).
5. Demand for know how and technology for the **optimization of logistics and quality control.**

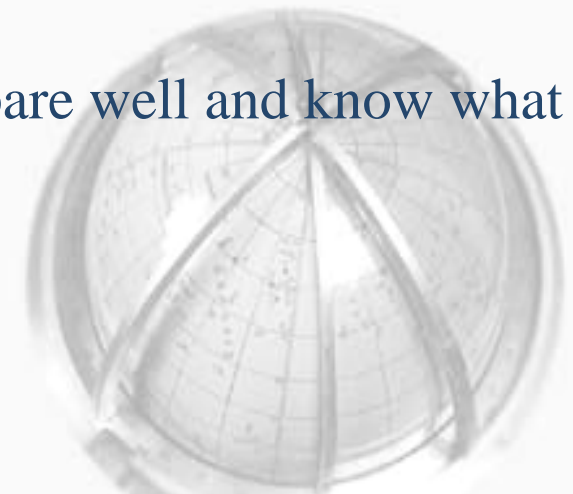


Conclusion and Questions – Why Russia??

1. The effects of the crisis have created a **new reality** on the Russian food sector.
2. Despite this new reality, the sector still offers plenty of opportunities for **flexible** foreign companies with a clear **added value**.
3. Companies that enter (or remain present on) the Russian market will be able to reap the **advantages** after the crisis.

BUT

4. Traditional problems will continue to exist so prepare well and know what you're doing!



Since 1999 Lighthouse assists Western companies in doing business in Russia. Throughout the years, Lighthouse has successfully assisted hundreds of companies from a wide range of sectors with their business development in Russia. Whether you need to start or increase your sales, set up production or do an acquisition, Lighthouse has the experience, the network and the team to help you reach your goals faster, cheaper and with less business risks. We are always happy to exchange thoughts with you about your business in Russia.

For further information you can contact us by using the coordinates below.

Contact Lighthouse

	Director	Jeroen Ketting	jeroen@thelighthousegroup.ru
	Client Relations and Information	Birgit von Oehsen	birgit@thelighthousegroup.ru
	Finance & administration	Elena Kabko	elena@thelighthousegroup.ru
Tel.:	+7 (495) 980 09 77		
Fax:	+7 (495) 502 92 86		
Website:	www.thelighthousegroup.ru		
Address:	Mytnaya Ulitsa 3, office 41, Moscow, Russia, 119049		