



Agriculture and
Agri-Food Canada

Agriculture et
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**International
Markets
Bureau**

MARKET ANALYSIS REPORT | FEBRUARY 2010



State of the Market

Agriculture and Agri-Food Sector Russian Federation

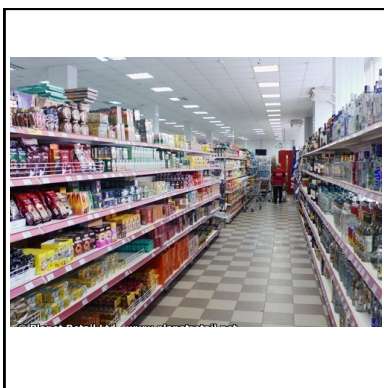
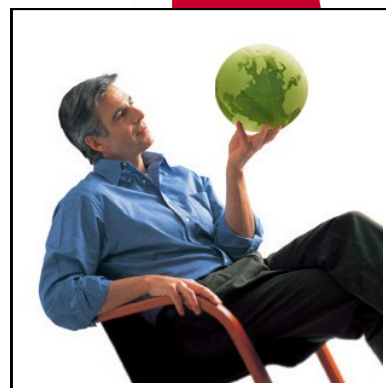


Photo courtesy of Planet Retail





► EXECUTIVE SUMMARY

Russia is one of the world's major markets for agri-food and fish and seafood products; it is the world's second largest agri-food importer among emerging markets, and fifth overall (counting the European Union as a single market). Its consumer market is now the eleventh largest in the world and is forecasted to become the fifth largest by 2020 (Euromonitor, 2008). Although growth slowed in 2009, Russia is still expected to outperform globally. Suppliers, investors and retailers are investing because they believe this market has long-term potential in almost every category (Datamonitor, 2008).

Russia's domestic agricultural industry has not kept up with growing domestic demand for agri-food products; the transition to a market economy remains incomplete. Russia will remain a net importer of agri-food products for some time to come.

Russian imports of agri-food, fish and seafood products are expected to continue to grow over the next few years, but possibly at a lower rate than the last five years. The combination of rising incomes, rising per capita consumption of food in general, including meats, fish and seafood products, and demand for greater variety and quality is generating opportunities for Canadian suppliers. Opportunities are spread widely across all segments of the industry.

The outlook for Russian imports, however, is complicated by the current global recession. Since the recession began in the middle of 2008, Russian consumers have cut back on spending, often shifting from premium to economy brands. However, it is expected that spending patterns will return to pre-recession levels once the downturn ends. It is also expected that Russian agri-food and fish and seafood imports, and the Russian economy as a whole, will begin growing again once the economic crisis has passed.



Source: Planet Retail

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Russia's imports of agri-food products from Canada, including fish and seafood, almost doubled from 2006 to 2008, reaching \$550 million.

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► THIS REPORT

This report outlines trends that are expected to continue in the Russian agri-food and fish and seafood market over the next 3-5 years, including:

- Overall growth;
- Continued growth in demand for both greater variety and enhanced quality;
- Consumption patterns converging with Westernized patterns;
- Strong growth in the food service sector in general and in medium-priced restaurants in particular;
- Continuing expansion of retailers and food service in cities beyond Moscow and St. Petersburg;
- Continuing challenges for retailers, food processors and food service operators in sourcing agri-food products.

The information accumulated for the purpose of this study points to opportunities for:

- large scale suppliers
- small and medium sized suppliers
- niche market operators

The following six areas are thought to be the best prospects:

- Meats
- Fish and seafood products
- Alcoholic Beverages
- Ingredients
- Packaged Food
- Animals and animal genetics

► RUSSIA: A STORY OF GROWTH

Over the past five years Russian imports of agri-food products have increased from US \$11 billion in 2003 to US \$32 billion in 2008, an increase of 187%. Russia is now the world's second largest agri-food importer among emerging markets, and fifth overall (counting the European Union as a single market).

This extraordinary growth reflects several underlying factors. Firstly, Russia's Gross Domestic Product (GDP) grew by 7% per year during this period, while the average disposable income increased by 80%. Moreover, according to Euromonitor, 48% of Russians are now considered middle class (annual disposable income between US\$10,000 and US\$ 25,000), growing from just eight million people in 2000 to 55 million in 2006. The Russian consumer market is now the eleventh largest in the world and is forecasted to become the fifth largest by 2020. (Euromonitor, 2008)



Source: Planet Retail

Having shifted from an oil-dependant economy to a consumer-driven one in recent years, Russia has become one of the world's most dynamic markets for a range of consumer goods and services. Despite its financial markets being hit hard by the economic downturn, Russia still has the potential to become one of the world's largest economies.

Russia's impressive growth has important implications for Canadian agri-food and fish and seafood exporters.



► SECTOR OVERVIEW

Russia has been a net importer of food for much of its history. In spite of its great size, Russia has relatively little area suitable for agriculture because of its arid climate and inconsistent rainfall. Northern areas concentrate mainly on livestock, and the southern parts of the country, as well as western Siberia, produce mostly grain. Reform of the agriculture sector has been slow and there is still much to be done. In 2008, Russia had a trade deficit in agri-food products of nearly US \$25.3 billion.

Russia's main agricultural region extends nearly 5,000 kilometres from the Central District, which borders Ukraine and Belarus, to the western part of Siberia. In 2005, for example, out of the roughly 133 million hectares (Mha) of arable land, 47 Mha of grains and oilseeds were harvested. The remainder is largely pasture and meadows for livestock grazing. Agriculture accounts for about 7% of Russia's Gross Domestic Product (GDP), considerably less than the industrial sector which contributes 40%. The major field crops grown in Russia, in order of production, are wheat, barley, sunflower, oats, rye, and corn.

Russian agricultural producers may be divided into three categories:

- 1) Former collective (state-owned) farms—these have been divided into approximately 25,000 units. Approximately half of these are reportedly bankrupt with many of them unlikely to turn into profit-making enterprises. About one quarter or more are profitable. In other words, profitability is fairly concentrated. Nevertheless, this group is responsible for the biggest portion of agricultural output in Russia, possibly as much as 80%. Russian businesses are making significant investments in many of the large enterprises in this category.
- 2) Small private plots—these are made up of approximately 16 million owners of plots of about .43 hectares each. While these holdings are small, it has been reported that they account for a sizable portion of agricultural output in Russia.
- 3) Private farms—these represent about a quarter of a million farmers. The average farm size in this group is approximately 70 hectares. Collectively, they account for approximately 5% of agricultural production in Russia.

Russian imports include a high proportion of high-value consumer goods; last year 61% of Russia's imports of agri-food products were in the consumer-oriented category, such as pork, pet food and poultry. Russian imports are also very diverse; last year's imports included 16 broad categories that amounted to more than US \$500 million in imports each, and 30 categories that were over US \$100 million each.

In 2008, Russia's top imports of agri-food products, in percentage terms, were:

- Meat (23%)
- Edible fruits and nuts (14%)
- Beverages (8%)
- Edible vegetables (6%)
- Prepared vegetable, fruits and nuts (5%)
- Dairy products, birds eggs and honey (5%)
- Sugar and sugar confectionary (4%).

The following countries were Russia's top agri-food suppliers in 2008 (market shares are in brackets):

- Brazil (13%)
- The United States (7%)
- Germany (6%)
- Ukraine (6%)
- Netherlands (5%)
- Argentina (4%)
- France (4%)
- China (4%).

In 2008, Russia's imports of agri-food products from Canada, including fish and seafood, reached US \$550 million, almost double its imports in 2006. A significant portion of Canada's agri-food exports to Russia are in higher value, consumer-oriented products, amounting to 52% of total agri-food exports to Russia in 2008. In the same year, Russia ranked fourth as a destination for Canadian exports of consumer-oriented products, ranking higher than China or any European Union (EU) country.



► MARKET AND SECTOR CHALLENGES

Since the early 1990's, the agri-food sector in Russia has been going through a transition from a planned economy to a market-based one. This transition continues today. The three major components of the Russian agri-food sector—primary agriculture, food processing and food retailing—have fared very differently during the transition. The primary sector has achieved modest progress, the processing sector has made substantial progress and the retail sector has undergone dramatic change.

Agriculture

While observers differ in their assessments of Russian agriculture's transition to a market-based system, there is general agreement that progress has fallen short of expectations. According to the World Bank, by 2005, Russia had only implemented about two thirds of necessary reform policies. Progress that depends on increased efficiency at the farm level is generally described as either modest or disappointing. While reports frequently point to inefficiency in Russian agriculture, with considerable evidence to support that conclusion, such observations of inefficiency should not mask the fact that some enterprises are operating profitably. Profitable agri-food enterprises include a portion of former state farms and a portion of private farms. Factors favoring progress include a substantial land base, a sizeable number of highly-educated and trained agricultural specialists and professionals, growing consumer demand and an influx of investment, both private and public. In addition, analysts such as William Liefert of the United States Department of Agriculture (USDA) note that Russia's trade in agricultural products and agricultural inputs have generally been consistent with comparative advantage in recent years, implying that progress has been made towards a market-based system. Liefert also indicates that Russia's comparative advantage in the future is likely to lie with bulk field crops such as grains and sunflower seeds, not with meat production.

While many reports focus on farm enterprise performance or on policy achievements, it must be borne in mind that Russian agriculture faces natural limitations as well, such as limited arable land and unreliable climatic conditions.

The Russian Government recently approved a US\$41 billion program for the development of agriculture for the period of 2008-2012. The broad objective of the program is to increase Russia's self-sufficiency in food. Specific objectives are sustainable rural development, increased rural employment, improved rural living standards, improved competitiveness of Russian agriculture and natural resource conservation. Russian officials expect agricultural production to increase by 20% between 2007 and 2012 as a result of the program. Meat production is one of the targeted areas.

The objectives of the program are understandable and the level of resources allocated to it, backed by a political commitment, will undoubtedly generate changes in the Russian agri-food sector. It is very likely that domestic output of agricultural products will increase over the next few years. However, the nature and extent of the resulting changes are difficult to foresee, particularly, the potential changes to Russia's trade in agri-food products. It is plausible that Russia would follow the same pattern as most agricultural producing countries by focussing on goods that can be produced competitively within the country and importing others. In fact, most of the main agricultural producing countries engage in two way trade in agri-food products. As the above discussion implies, Russia is likely to have a comparative advantage in some products and a comparative disadvantage in others. Consequently, Russia is likely to be an agri-food importer, as well as an exporter, well into the future. This view is reflected in a recent USDA assessment, "Russia's Growing Agricultural Imports," May, 2009.

Food Processing

In contrast with the primary sector, the food processing industry has been experiencing considerable growth, with some reports indicating growth rates of 15-20% annually in recent years. Some observers have estimated the number of food processing plants in Russia at 8,000 to 10,000. Many have upgraded their technology and equipment over the past five or six years. Demands from the retail sector for high quality products, combined with competitive pressures emanating from foreign multinationals operating in the country, is pushing the sector forward. According to observers, domestic sources of raw resources and specialized ingredients for meat, bakery, confectionary, juice, and dairy processing have not kept pace with the expansion of the sector and are unlikely to do so for the foreseeable future. Many Russian food processors are now focussing on international quality standards and seeking quality ingredients. A combination of domestic and foreign investment has produced a fairly dynamic sector, providing a market for inputs and ingredients.



Food Retailing

By 2020, Russia is expected to take over from France as the largest food and grocery market in Europe. Analysts have recently made the following observations about this market:

- value is increasing faster than volume
- consumers are becoming more demanding in terms of variety and quality
- more and more competition will be based on upgrading quality, improving packaging and launching new products.

The growth in demand for higher quality food, in greater variety, is driven primarily by rising disposable incomes. The rise in disposable incomes is, in turn, being fuelled by strong economic growth, spread over a number of sectors. In addition to the overall growth in demand for food products, the variety of products in demand is also striking.

The growth of modern marketing formats has been gradually displacing traditional retail operations, similar to what has already occurred in Western Europe and North America. The first supermarkets appeared in Russia in the early 1990's and, by the end of 2005, there were already approximately 2,600. Hypermarkets were introduced in 1997. Only recently have they shown rapid growth. There has also been growth in convenience stores and discount supermarkets.

The modernization of the food retail industry in Russia and the influx of foreign supermarket chains have led to the gradual modernization of supply chains. In many cases, Russian supermarket businesses are making efforts to develop increased transparency and efficiency in their supply chains. This creates conventional, open, legitimate business environments and displaces a legacy and stigma of corruption previously associated with supplying the Russian market. Furthermore, the aggressive expansion plans of Russian-owned and international supermarket chains gives real opportunities for their suppliers to access larger networks, as more and more stores spring up in Russian cities.

The supply channels to food retailers in Russia are extremely competitive. In recent years, supermarkets have caused a rationalization of the supply chain and eliminated many intermediaries and smaller distributors and suppliers. However, unlike many developed markets, Russian supermarkets do not operate "category management" systems that favour fewer, trusted, long-term suppliers. In most instances a "panel system" is in operation, whereby many suppliers pitch to supermarket buyers for their business. This structure is geared to obtaining the lowest price for products and creates a trading environment where suppliers must prove themselves week in, week out.

In the long term, supermarkets will stimulate demand for:

- "convenience" products
- new / innovative products
- low cost / value / budget products
- premium / healthy products (currently limited by consumer product knowledge)
- international brands (currently limited to a few product groups e.g. drinks / confectionery)
- own brand products (currently limited to a few lines in larger supermarket groups).

► CONSUMER AND MARKET TRENDS AND DEVELOPMENTS

Overall growth is expected to be a dominant trend for agri-food in the Russian marketplace. Despite the current effects of the economic downturn, consumer spending habits in Russia are likely to maintain healthy growth, due to increased awareness of the quality and variety of goods available, and the Russian consumer's growing buying power.

Growing disposable incomes in all segments of the Russian population fuelled consumer demand in virtually all consumer markets pre-recession. Annual disposable incomes grew by 74% between 2002 and 2007, reaching US \$4,972 per capita (Euromonitor, 2008).

Regardless of the effects of the financial crisis, this noticeable increase has had a strong impact on the lifestyles of consumers at all income levels, positively affecting buying and consumption patterns for Canadian suppliers.

To follow are the specific trends and developments to watch in the Russian market for the future.



Quality and Variety

Consumer spending on food grew by 70% between 2002 and 2007, reaching US \$1,250 per capita in 2007 (Euromonitor, 2008). As many Russian households spend over one third of their budget on food and non-alcoholic drinks, expenditures in this industry remain the most important in consumer spending. Rising income levels and greater variety in the marketplace have sensitized middle-class and affluent Russians to the quality of the food they buy, thus increasing demand for both greater variety and enhanced quality.

As more and more Russians travel around the world for both business and leisure, they are increasingly exposed to international trends and ethnic foods. As a result, traditional buying and eating habits are changing to accommodate greater curiosity and spending power. Middle-income consumers are increasingly buying premium branded goods such as value-added foods, meats, fresh foods, fish and seafood, as well as premium alcoholic beverages.

Euromonitor market studies indicate that Russian consumers prefer international brands due to their perceived superior quality. Advertising increasingly plays an important role in the grocery choices of consumers, as the variety available in each category of goods has grown considerably. This increase in demand has caused brand competition to become more intense, thus amplifying the need for companies who wish to compete in the Russian market to invest in packaging formats and labelling designs that are appealing to Russian consumers. Consistent quality and advertising among international competitors has convinced Russian consumers that it is worth paying a premium for a well-known brand.

Health-Conscious and Convenience Foods

As a result of changing eating habits due to an increased awareness of the health risks associated with the high fat and salt content of traditional Russian foods, healthy foods are becoming increasingly popular, particularly among younger consumers.

As more people become wealthy and health-conscious, the market for diet, organic and fresh foods will grow rapidly, commanding premium prices, specialty stores and dedicated supermarket sections.

At the same time, the acceleration of lifestyles has led to a desire to reduce the time spent cooking and has resulted in greater use of processed and pre-cooked foods, as well as snack foods. Some Russian consumers have shown a preference for fast food and convenience foods such as ready meals.

The following tables outline the growth in consumer expenditures on food in recent years within the Russian market:

Russian Consumer Expenditure on Food

Rb billion	1995	2000	2002	2004	2006	2007
Bread and cereals	706.6	679.5	678.9	749.0	734.8	764.3
Meat	1,137.5	1,099	1,195.3	1,209.9	1,351	1,428.5
Fish and seafood	189.6	209.7	229.5	242	273.0	289.3
Milk, cheese and eggs	767.0	637.6	621.6	656.8	680.0	709.3
Oils and fats	129.3	125.8	124.3	103.7	85	88.6
Fruit	241.3	201.3	219.9	253.5	271.6	286.6
Vegetables	301.6	285.2	306	311.1	332.2	350.7
Sugar and confectionery	517.0	495.0	334.7	311.1	268.7	264.6
Other food	126.8	75.8	84	79.1	108.8	107.2
TOTAL	4,116.7	3,809	3,794.2	3,916	4,105.1	4,289

Sources: National statistical offices, OECD, Eurostat, Euromonitor International. Note: Constant value at 2007 prices.



Russian Consumer Expenditure on Food (% Analysis and % Growth)

% analysis / % growth	1995	2000	2007	1995-2007	2000-2007
Bread and cereals	17.2	17.8	17.8	8.2	12.5
Meat	27.6	28.9	33.3	25.6	30.0
Fish and seafood	4.6	5.5	6.7	52.6	37.9
Milk, cheese and eggs	18.6	16.7	16.5	-7.5	11.2
Oils and fats	3.1	3.3	2.1	-31.4	-29.6
Fruit	5.9	5.3	6.7	18.8	42.3
Vegetables	7.3	7.5	8.2	16.3	23.0
Sugar and confectionery	12.6	13.0	6.2	-48.8	-46.5
Other food	3.1	2.0	2.5	-15.5	41.3
TOTAL	100.0	100.0	100.0	4.2	12.6

Sources: National statistical offices, OECD, Eurostat, Euromonitor International. Note: Constant value at 2007 prices.

Changing Retail Formats

As the grocery retailing landscape in Russia shifts toward modern retail formats, Russian consumer buying habits are changing in terms of where they shop and how they buy.

According to Euromonitor International's retailing research, hypermarkets became the fastest growing retail format in Russia during 2006 and 2007, with value sales in local currency growing by more than 70% during that period.

As a result of the intensive development of these new retailing formats, volume consumption of fresh food rose by nearly 8% between 2005 and 2007, reaching 5.9 million tonnes in 2007. This growth was led by sales of fresh meat and fruit, up by 14% and 15% respectively, and the key vegetables sector, which was up by 8% (Euromonitor, 2008). Traditionally, fresh meat and other fresh foods were mainly sold through small independent grocers where the food quality was very inconsistent and where 30-40% of food product labels did not accurately describe the content; this, in turn, led Russian consumers to become sceptical about the quality of food sold by these retailers in general.

Nonetheless, the rapid expansion of chained hypermarkets and supermarkets in different regions of Russia, typically distributing higher-quality products and a wider product assortment, has stimulated consumption of various kinds of foods in recent years. This development may point to an underlying trend toward the consumer placing greater trust in modern retail formats than in traditional grocery channels, thus suggesting that the potential for private label sales within the Russian market is growing.

Since 2008, large global retailers such as Wal Mart have expanded into the Russian market leading to a more standardised approach to mass retailing and more reliable product quality. Competition is also intensifying, particularly with the expansion of numerous low-cost retailers such as Ramstore and Kopeyka, which drive down prices across many categories of goods and services.



Foodservice

The foodservice sector is expected to continue to grow—both within and beyond Moscow and St. Petersburg. Russia's foodservice market is developing at an impressive pace due to increasing consumer incomes and a growing tourist industry.

Expansion of the foodservice sector continued in 2008, with growth in regions beyond Moscow and St. Petersburg. Consumers in these cities demand greater variety and innovation of the sector, while growth in other regions supports the development of the less expensive fast food segment of the industry (Euromonitor: Packaged Food—Russia, 2009).

There has been strong growth in foodservice, particularly for fast food outlets, street stalls, kiosks and cafés. The emergence of the high-end restaurant culture is also leading many Russians to enjoy rare delicacies which, in turn, stimulates demand for more exotic foods. Additionally, observers have indicated an increase in the development of medium-priced restaurants, which will open another growing market for premium food products. The growing number of ethnic restaurants has spurred demand for imported food products and has resulted in their presence on supermarket shelves (e.g. nacho chips and dipping sauce).

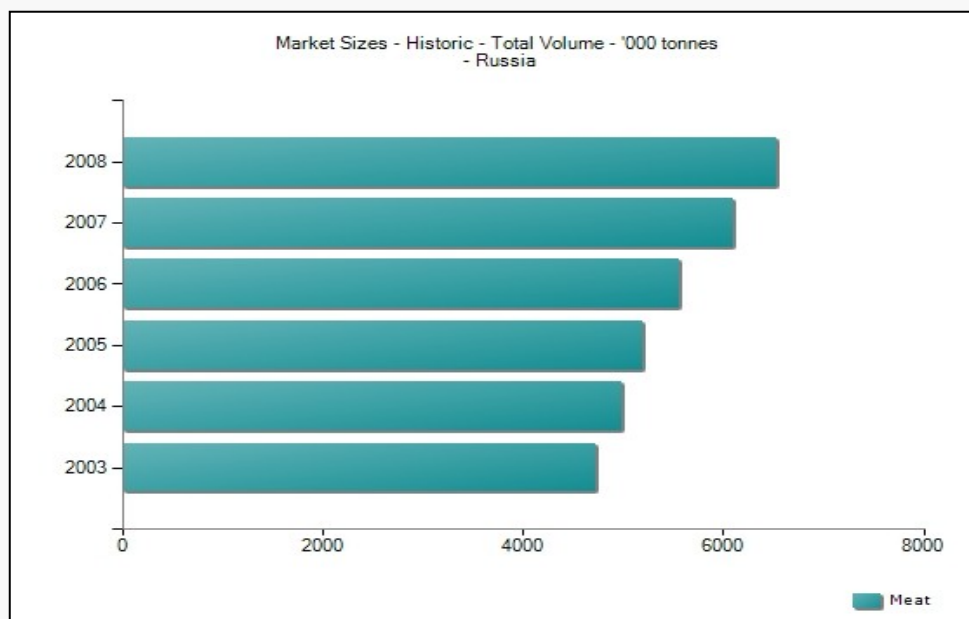
The premium foodservice sector presents market entry opportunities for small and medium-sized exporters of products such as wine, quality meat and specialty seafood products. According to most observers, the majority of agri-food products purchased by the food service sector are imported, nearly 90% according to a recent USDA report.

► SECTOR OPPORTUNITIES

Economic development will continue to push levels of personal income and encourage the consumption of a wider range of foods, which will become more affordable and more sought-after. There will likely be opportunities for suppliers of all sizes, as well as niche market operators. The following six areas are thought to be the best prospects for Canadian suppliers.

Meats: poultry, pork and pork products, beef and beef products, and specialty meat

Stagnating domestic meat production in Russia and the increased consumption of meat, which is expected to rise by 30% from 2007 to 2012, are expected to create a wide range of opportunities for many food producers—from the commodity trade to full-processed food lines (Euromonitor, 2008). According to forecasts by Euromonitor International, total meat consumption will reach almost 12 million tonnes by 2012.



Source: Euromonitor International

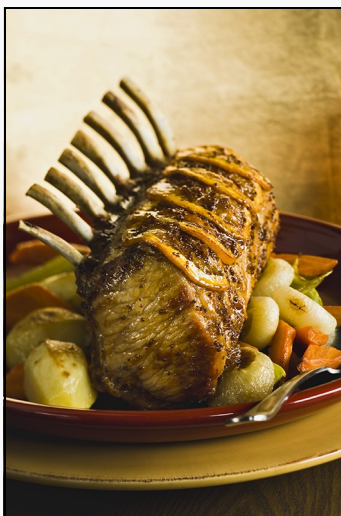
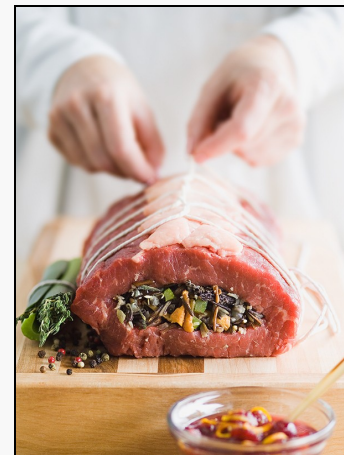


With volume growth of 13% over 2005-2007, chilled, processed meat saw the fastest development compared to other processed meat categories, according to Euromonitor International's packaged food research. This positive performance is attributable to a number of factors, most notably the perception that chilled, processed meats offer more nutritional value than canned/preserved and frozen alternatives. This perception is no doubt fuelled by an overabundance of new, chilled, processed meat products being positioned on the health and wellness platform. Reduced-fat variants quickly proved popular with consumers, and are expected to play an increasingly important role over the next five years.

In addition, chilled, processed meat producers have begun to invest in new packaging formats and labelling designs; while this was partly due to a desire to distinguish their products from those of their rivals, it has also been an effective response to consumer concerns over food safety.

While almost 90% of chilled, processed meat products sold in Russia are manufactured at local meat processing plants, multinational brands are becoming more popular, particularly in the premium segment. With volume sales likely to grow by more than 30% from 2007 to 2012, this presents huge opportunities for many more multinational meat producers, although competition is set to intensify as many local meat manufacturers rapidly upgrade their production processes, improving the quality of their products and brand-building.

According to the Global Trade Atlas, Canada is ranked fifth overall for total meat exports to Russia. Major competitors include Brazil, the United States, Germany and Australia. Stable growth levels have been achieved by Canadian exporters in recent years; however, competing countries have been more aggressive in entering the Russian marketplace. Important increases in exports and market share levels have been identified for Australia, Germany and the United States, while Canada has been increasing exports at an increasingly steady pace year-on-year.



More specifically, Canada is ranked seventh for total poultry exports, fourth for pork and related products, and ninth for beef and related products. Poultry exports have increased in recent years; however, they still represent lower volumes than beef and pork exports. Beef exports have demonstrated strong growth in recent years, with Canada acting as a strong competitor to other countries with similar growth rates, such as Australia, Uruguay and the United States. Within the pork sector, players such as the United States and Germany have demonstrated stronger growth levels than those of Canadian companies in recent years, resulting in stagnant market share levels for Canadian pork suppliers. Although exports are increasing yearly in these sectors, there is room for Canadian companies to gain market share.

Overall, healthy growth rates in Canadian meat exports indicate a consistent preference for Canadian meat products on behalf of Russian buyers and consumers. As the high-end restaurant culture continues to emerge, demand for imported marbled beef, beef fillets, lamb and veal will continue to increase, which in turn will lead to steady growth for imported meat (including meat offal). Other imported exotic meats, such as rabbit, kangaroo and ostrich, for example, are also increasingly popular among wealthier Russians, thus providing further opportunities for exotic meat exporters.



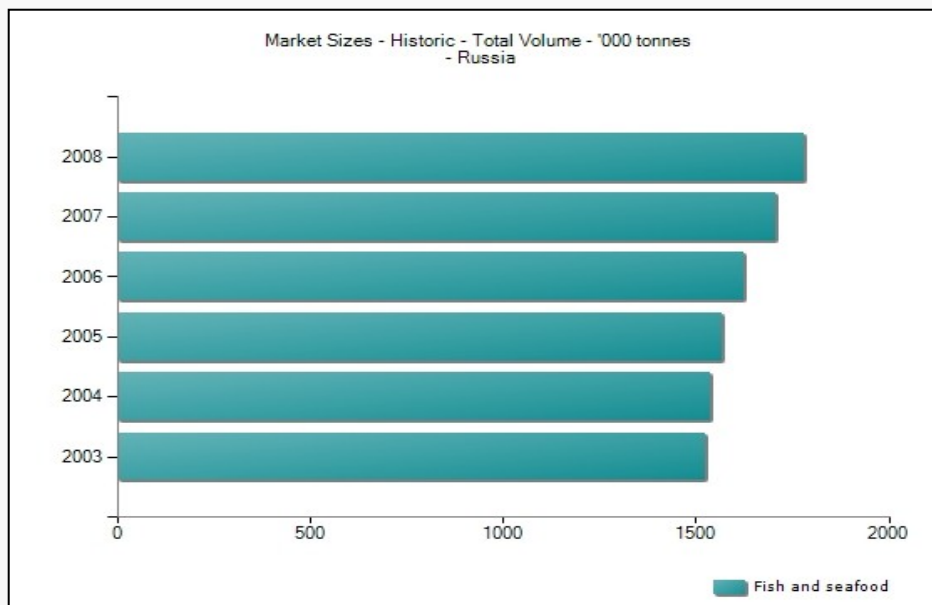
Fish and Seafood Products



Fish and seafood consumption is estimated to be increasing at a rate of 17% per year. Growth in the ready-to-eat segments, such as shrimp, crab, scallops, squid, and mussels, has been estimated to be 30% annually. The fish and seafood delicatessen market is also growing and thought to be far from saturation; local markets are carrying a full range of products covering all price ranges.

According to a USDA report, the demand for high quality products has led some retailers to launch new premium products in the market. As a result, the market for fish snacks is growing in tandem with the rising snack market in general (ACNeilson). The distribution of seafood sales is approximately 30% through markets/stalls, 45% through local shops, and 25% through supermarkets, although the latter are growing rapidly. The key species comprising this market are herring at 27%, pollock at 26%, mackerel at 18%, salmon and trout at 10%, and others at 19%.

While Russia is a significant fish and seafood exporter, it remains a net fish and seafood importer, with imports growing at a strong rate. Russia's imports of fish and seafood products in 2008 were \$2.4 billion, up 20% from 2007. This growth trend is expected to continue for some time. Russia's rising fish and seafood consumption is generally attributed to both rising incomes and changing consumer preferences that are putting greater emphasis on health benefits associated with fish and seafood products.



Source: Euromonitor International

Growth in Russian imports of fish and seafood products from Canada has been impressive; fish and seafood imports from Canada rose from \$41 million in 2005 to \$95 million in 2008. Key Canadian exports include cold water shrimp, mackerel, and hake.

The fish and seafood sector has proven to be a promising area of opportunity for Canadian suppliers specializing in fish, crustaceans, mollusks and other aquatic commodities. Trade statistics have placed Canada sixth for total exports to Russia in this sector, after Norway, China, Vietnam, Denmark and Chile.

Canada's total exports of fish and seafood have increased every year since 2003 and are expected to continue to grow. Although exports have decreased in 2009, demand for fish and seafood is expected to remain an area of opportunity and growth once the economic crisis has passed.



Alcoholic Beverages

Expenditures on alcoholic drinks in Russia grew by 25% from 2002 to 2007, reaching US \$71 per capita (Euromonitor, 2008). As younger consumers begin to prefer beer, wine and alcoholic cocktails as opposed to vodka and other strong spirits, the patterns of alcohol consumption in Russia are changing. Vodka is commonly seen as a poor and middle-class drink, while the rich increasingly opt for imported drinks, which are perceived as more prestigious.

Today, much of the vodka consumed has been replaced by beer. Beer is widely available in Russia and the competition in this market has become intense, with both major domestic players, such as Baltika from St. Petersburg, and international ones, such as Heineken. Beer is consumed by all sections of the population.

Wine has also become a fashionable drink over the last decade and Russian consumers have increasingly learned to differentiate between varieties and grapes. In bigger cities and towns the taste for alcohol is becoming more discerning, with wine from both the 'old' and the 'new' worlds becoming increasingly popular. The tables below indicate the areas of growth in alcoholic beverages in recent years in Russia:



Russian Consumer Expenditure on Alcoholic Beverages and Tobacco

Rb billion	1995	2000	2002	2004	2006	2007
Alcoholic drinks	215.4	209.7	211.5	243.6	239.3	256.2
- Spirits	141.7	130.9	134.5	153.5	150.8	161.8
- Wine	35.1	34.7	33	39.5	38.7	40.1
- Beer	38.7	44.1	43.9	50.6	49.8	54.3
Tobacco	86.2	100.7	96.1	104.4	103.9	114.9
TOTAL	301.6	310.4	307.6	348	343.2	371

Russian Consumer Expenditure on Alcoholic Beverages and Tobacco (% Analysis and % Growth)

% analysis / % growth	1995	2000	2007	1995-2007	2000-2007
Alcoholic drinks	71.4	67.6	69	18.9	22.1
- Spirits	47	42.2	43.6	14.2	23.6
- Wine	11.6	11.2	10.8	14.3	15.4
- Beer	12.8	14.2	14.6	40.2	23.1
Tobacco	28.6	32.4	31	33.3	14.1
TOTAL	100	100	100	23	19.5

Sources: National statistical offices, OECD, Eurostat, Euromonitor International. Note: Constant value at 2007 prices.

In 2008, Canada was ranked the 22nd largest exporter of beer into the Russian market and continues to see growth on a yearly basis. Competing countries such as Italy and Lithuania have demonstrated high growth levels in the last two years, clearly demonstrating the demand for imported beer. Other players such as Japan, the United Kingdom, Austria, China and Armenia are also showing healthy growth levels, thus intensifying the level of competition within the Russian market. Interestingly, market share levels in beer exports to Russia for the Czech Republic, Belgium, Japan and the United Kingdom have increased at a faster pace than that of competing countries.



Ingredients

Ingredient companies stand to benefit from the booming meat sector in Russia, as a result of economic development and the increasing sophistication of consumer palates. According to Euromonitor, the quantity of herbs used in chilled processed meats has increased by more than 50% in the last five years to slightly more than 19,000 tonnes in 2007. Observers state that domestic sources of raw resources and specialized ingredients for meat, bakery, confectionary, juice, and dairy processing have not kept pace with the expansion of the sector and are unlikely to for the foreseeable future. As a result, a dynamic and growing food processing sector with a scarcity of high quality inputs and ingredients, creates many opportunities for Canadian suppliers.

Due to the emergence of numerous ethnic restaurants, many Russians now wish to experiment with foreign cuisine at home and are now looking for foreign ingredients. From a retail point of view, this creates additional opportunities for the ingredients sector.

Packaged and Specialized Foods

The packaged food market in Russia, the fastest growing in the world, is approaching US\$150 billion in value. Growth in this sector was boosted by rising incomes, a trend towards value-added products and the growing availability of imported products, as well as the development of modern retail formats. Products in this sector include: meal replacements, ready meals, snack food, dairy products (cheese), confectionery products, baked products (bread, pastries), frozen processed food, pet food and baby food.

This industry sector, led mostly by major international and local players in Russia, has increasingly seen consolidation between companies and manufacturers due to tough competition. Mergers and acquisitions have become more and more popular among interested exporters, as most large manufacturers have the means to effectively promote their brands and often already have a loyal consumer base.

The packaged food market provides opportunities spread over a wide range of product categories. Sales within the sector increased on average by more than 20% per year between 2003 and 2008 and are expected to grow by more than 8% annually over the next five years (Euromonitor, 2008). Within packaged foods, dairy products became the largest sector, but the strongest growth was seen in convenience foods such as frozen processed foods, ready meals, sweet and savory snacks and baby food.

Pet food has also experienced strong growth, growing by 275% in value terms between 2002 and 2007, to reach US\$ 1.4 billion (Euromonitor, 2008). Despite this noticeable increase in pet food imports, Canada's market share has decreased since 2006, thus demonstrating an area of opportunity to sharpen Canada's competitive edge in this sector. For additional information on the pet food market in Russia, see the market indicator report, [Pet Food in Russia](#), which is available on the Brand Canada website: www.marquecanadabrand.agr.gc.ca.



The increased demand for better quality has also supported growth in meal solutions, canned/preserved vegetables, frozen processed vegetables and frozen fish and seafood. The rising interest in health and wellness, and the increased demand for prepared products will, in turn, create opportunity for high-end products and multinational brands.

Animals and Animal Genetics

The Russian Government recently approved a \$US 41 billion program for the development of agriculture for the period 2008-2012. Russian officials expect agricultural production to increase by 20% as a result of the program. As one of the targeted areas, meat production has created multiple opportunities for Canadian exporters of live animals and animal genetics. According to the Global Trade Atlas, Canadian exports of live animals has tripled in the last three years, demonstrating increased demand for animals and, thus, opportunities within this sector.



► OUTLOOK

The outlook for Russian imports of agri-food and fish and seafood products is complicated by the current global recession. Russia's economy, personal incomes, consumption and imports have all been affected, diverting it from the growth patterns that have been observed prior to the recession. Since the recession began in the middle of 2008, Russian consumers have cut back on spending, often shifting from premium to economy brands. Consumer demand has shifted dramatically toward lower-priced goods, as consumer sentiment is influenced by falling disposable incomes, rising unemployment and wage arrears. This has forced cash-strapped Russians to shop more at budget chains. This trend is evident in the increased sales of discount food retailers (Euromonitor: Packaged Food—Russia, 2008).

Nonetheless, it is expected that spending patterns will return to pre-recession levels once the recession ends. It is also expected that Russian agri-food and fish and seafood imports will return to growth once economic downturn slows and the Russian economy returns to another growth period. While Russian agri-food and fish and seafood imports are expected to return to a growth path, the rate of growth is not expected to be as high as it was prior to the recession, partly due to increased domestic production (USDA, "Russia's Growing Agricultural Imports," May, 2009).

► TRADE POLICY AND ACCESS ISSUES

The Russian Federation's impending accession to the World Trade Organization (WTO) will set limits on the amount of trade-distorting domestic support that the government can provide to the agriculture sector. In addition, adherence to a range of WTO agreements, such as the Agreement on the Application of Sanitary and Phytosanitary Measures (SPS) and the Agreement on Technical Barriers to Trade, will require the Russian Federation to adopt more consistent and transparent import measures.

For exporters of agri-food products and fish and seafood, it is important to be aware that there are still a number of significant challenges associated with selling to the Russian market. For example, due to the rapid modernization of Russia's domestic legislation and regulatory systems, Russian importers may not always be aware of the current market requirements (e.g., labeling) for certain foods and beverages, as well as other import procedures which must be followed.

In addition, an increase in food-safety violations and animal and plant disease outbreaks in a number of exporting countries, has meant that the Russian Federation—one of the world's largest net importers of food—has become increasingly concerned with the efficacy of animal and plant health controls within its supplier countries. Russian authorities are becoming more vigilant in enforcing animal and plant health-related requirements at border entry points.

As with other markets, exporters are strongly advised to consult with Canadian government officials, in addition to potential importers and customers, to verify that their product may be exported to the Russian Federation and to determine the requirements that their product must meet in order to be distributed within the Russian market.



▶ ADDITIONAL INFORMATION

Trade Events

PRODEXPO 2010
February 8-12, 2010
ZAO Expocentr
Moscow, Russia
Internet: <http://www-eng.expocentr.ru/en/>

World Food Moscow 2010
International Food, Beverage, Food Processing and Packaging Exhibition
September 14-17, 2010
Krasnaya Presnya Expocenter
Moscow, Russia
Internet: <http://www.world-food.ru/eng>

Russian Agricultural Exhibition "Golden Autumn" (Annual)
October 2010
Moscow, Russia
Internet: <http://www.apkvvc.ru/engaut.htm>

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Ms. Marina Fomitcheva
Trade Commissioner
Moscow, Russia
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Useful Internet Sites

<http://www.infoexport.gc.ca/ie-en/MarketReportsAndServices.jsp>

<http://www.canadabusiness.ca/eng/105/165/>

<http://www.ats-sea.agr.gc.ca/intro/index-eng.htm>

<http://www.inspection.gc.ca/english/directory/offbure.shtml>

http://www.edc.ca/english/8522_contact_us.htm

<http://www.fas.usda.gov/ffpd/Fish-Circular/attaches.html>



► KEY RESOURCES

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Global Trade Atlas. www.gtis.com/GTA/.

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Organization for Economic Co-operation and Development. www.oecd.org.

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The Government of Canada has prepared this report based on primary and secondary sources of information. Although every effort has been made to ensure that the information is accurate, Agriculture and Agri-Food Canada assumes no liability for any actions taken based on the information contained herein.

State of the Market—Russian Federation

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