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Retail Food Sector

Report

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Report Highlights:

The Estonian food market holds potential for imports of a wide range of high-value packaged goods targeted to higher/middle income level groups, increasing numbers of tourists and growing expatriate community. The fast-developing consolidation of retail outlets through investment by large Scandinavian chains may provide new opportunities for exporters who can successfully connect with these companies. The newly enforced import tariff schedule may disadvantage some competition from the United States as tariffs for European countries are set at zero while US imports face MFN rates. On average, consumer demand remains price sensitive. Trade and investment opportunities may provide free access to the EU market once Estonia accedes to the European Union.

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I. MARKET SUMMARY

The process of consolidation of retail chains and inflow of Scandinavian/European retailers has recently increased the competition and contributed to the fast growth of the Estonian food market. In 1999, the domestic retail food trade amounted to US\$ 795 million, an increase by 40% compared to sales of US\$565 in 1997. Food sales accounted for almost 36% of total retail turnover. Opportunities exist for new products and market entrants - - particularly for products marketed through the developing retail chains.

Consumption patterns and demand for imported food products are affected by an increasing expatriate community, fast growing tourism and the rise in consumer purchasing power. Imports accounted for nearly 35%, or US\$ 286 million of the Estonian food retail market. Imports are adding to the variety of products on the market. However, estimates still point to some 15% of food supplies being smuggled into Estonia from Central and Eastern European countries in an attempt to avoid import charges.

Since mid nineties, sales of food in supermarkets and shopping centers have increased considerably, influenced by fast changes in market structure and reduction of non-registered turnover. In terms of turnover, independent groceries and traditional markets led the sector with combined sales totaling US\$ 372 million. In 1999, the number of retail food stores totaled 2,680. In addition, food was sold in 61 supermarkets, 755 kiosks and 112 convenient stores.

Table: Value of retail food sales by sub sectors, 1999

Sub-sector	Food Sales (\$US Mil)
Supermarkets/Hypermarkets	185
Convenience Stores/Gas Marts/ Kiosks	238
Outdoor markets/Independent Groceries	372
Total	795

Estonia maintained very healthy growth in 2000, although it experienced an economic downturn in 1999, caused by the Russian financial crisis. A 6-7% rate growth for the Estonian economy - - is supported mainly by external demand, and the related growth in investments and household spending. The prices of goods and services in 2000 rose on average by 4%, a slight increase compared to 3,2% inflation in 1999. In 1999, per capita GDP amounted to US\$ 3,244, which is considerably lower than average for EU countries. The official unemployment rate was 4,5% of the total labor force.

Estonia was among the first wave of Central and Eastern European countries offered EU accession negotiations in 1999. Trade and investment opportunities in Estonia include free access to the European market, once Estonia becomes an EU member in 2003-2005. Further support for healthy trade and expansion of investment come in the wake of Estonia's WTO membership, which was effected in December 1999.

Customer profile

Consumer preference differ significantly among various income, age and ethnic groups. A preference for new products is strong among the younger population, but significant number of consumers remain "tasting level" buyers. There are long-established consumer preferences for domestic fresh products with short shelf lives and which are free from

additives. According to surveys, about 80% of consumers prefer domestic food products.

Overall population numbers are on a decline, due to negative birth rates and emigration of the young non-Estonians. As of mid 2000, there were 1,376 million inhabitants in Estonia, a decrease by almost 8% since 1990.

A negative effect of Estonia's fast economic reform has been a skewed distribution of income. Certain segments of the population presently function at or near the poverty level. The Estonian population is aging and reflects the approach to retirement age of the post-war baby boom generation. Of total population, 26,7% are retired. The average pension of \$103 per month allows for almost no variety in food purchases. Nearly 30% of population lives in rural areas. In many households, farming provides family staples mainly due to limited income and purchase power.

Since 1995, incomes have stabilized and have increasingly been able to meet more of consumer's basic needs. The average gross monthly wage in the public sector averaged US\$ 400 in 2000, while the average monthly per capita disposable income of households amounted to US\$ 134. Food expenses dropped to 33% of disposable income. The consumption volumes of most food products are smaller than the optimum basket necessary for healthy nutrition. Women account for 48% of nearly one million economically active people and contribute to the increased demand for meals consumed away from home. Estonians spend approximately 9% of their total food dollar on eating out. Prepared home meal are preferred to out-of-home dining in nearly half of the families. With a large proportion of two-income families, Estonian customers prefer meals that are quick to prepare. Therefore, prepared, frozen and convenience food should be a key focus of US exporters. Note, however, that stoves refrigerators, and freezers have much more limited capacity than is the norm in the U.S. and much of Western Europe.

Advantages and Challenges Facing U.S. Products in Latvia

Advantages	Challenges
U.S. products are considered safe and good quality. The general image of U.S. products is positive.	Long established consumer preference for domestic fresh products without additives.
The retail sector is looking for high processed food imports.	Based on the newly effective import tariff schedule, U.S. exports face MFN rates compared to zero duties for exports from European Union and FTA countries.
Purchasing power of the population is on the rise.	Estonia is a small target market for US products. Most Estonian customers are conservative with a low level of purchasing power that doesn't allow for choice.
The country is viewed as a gateway to larger markets in Northwestern Russia, Ukraine and Belarus.	High competition on the local market between domestic producers and increasing imports from EU and Baltic FTA neighbors.
Estonia joined the WTO in December 1999.	High distribution and shipping costs.

SECTION II. ROAD MAP FOR MARKET ENTRY

A. Supermarkets Sector

As consumers in Estonia become more sophisticated, convenience of shopping and expanded choices have become major considerations. The result is the emergence of large self-service shopping centers in the outskirts of the capital of Tallinn, as well as other larger cities during 1999/2000. Supermarkets have become more influential, especially in suburbs than small businesses. On average, supermarkets carry 3,500-7,000 items. Since the mid nineties market consolidation has been occurring and sales of food in supermarkets have increased considerably. Supermarket sales were estimated at US\$ 185 million in 1999.

Table: Profiles of Supermarkets

Retailer Name	Ownership (country)	1999 Sales (\$US Mil)	Number of Outlets, end 2000	Location City/Region	Purchasing Agent Type
Rema/Spar	Norwegian/ Estonian/ Swedish/ Finnish	38	24	Capital/ Regional Centers	Direct Importer
Maksimarket	Finnish/ Estonian	17	4	Capital	Direct
Konsum	Swedish/ Estonian	9	11	Capital/ Regional Centers	Direct/ Agent
Saastumarket	Estonian	8	3	Capital	Direct Importer
A-Selver	Estonian	6.5	5	Capital	Direct Importer

The Saastumarket (Saving Market) chain stakes its draw on low prices at the expense of a broader selection of choices and fancier stores.

Kesko Eesti, the leading retail chain in Finland, plans to build a comprehensive network of grocery stores in Estonia. There are two SuperNetto stores operating in Tallinn at present, and the next stores will be opened in Tartu in the spring of 2001. Kesko's target is a market share of 20-25% , US\$ 3 billion in the Baltic grocery market.

The second Rimi supermarket opened in Tallinn in fall 2000. The Norwegian company is strengthening its presence in the Baltics, despite tight competition.

Large supermarkets tend to provide different additional services to consumers offering ready-to-cook prepared foods, cafeterias, home-meals replacement and party trays. Increasingly these markets are housing gift and parcel wrapping, flower shops, currency exchange and pharmacy services. In addition large supermarkets offer dry-cleaning, shoe repair and cleaning, banking, insurance, film developing, and video rental services. Internet sales are becoming more popular among the young population. Wholesale clubs do not yet exist in Estonia.

Entry Strategy

New market entrants will have to be aggressive to overcome the established presence of European suppliers of consumer oriented products. Several constraints have contributed to the small market presence of U.S. foods so far:

Trade terms from U.S. companies tend to require advance payment of up to two-months.

An aversion to the assumption of exchange rate risks.

Minimum quantities offered have often been too large for the small Estonian market (e.g. full container shipments).

A perception that persists among Estonian importers that landed costs of U.S. products will be higher compared to European products - - due to added transportation costs.

A perception that U.S. exporters are simply too far away to service the Estonian market.

U.S. products traditionally have lower customer awareness due to fewer promotional activities than those of competitors.

We advise that market entry strategies include:

Market research in order to estimate product opportunities.

Locating an experienced distributor or independent reliable agent with strategic distribution channels, to advise on import duties, sanitary regulations, and labeling requirements.

Advance calculation of the landed cost of a product in order to make price comparisons vis-a-vis competitors.

Initiation of personal contact is advisable in order to discuss marketing. Negotiations of marketing strategies should include funding offers for advertising, slotting allowance, in store promotions and tasting, consideration of trade fair participation to raise awareness of the product.

Marketing strategies should emphasize the cultivation of a relationship with a local company or importer who will then promote any new product. As a result of the fast-developing consolidation process, perhaps the most effective strategy would be to connect with parent companies in Scandinavia.

Distribution

Estonia's distribution system is the most advanced among the Baltic States. Cash and carry operations are popular, although distributors are moving toward direct deliveries with their own sales force and delivery trucks to service retail groceries, and chains. This type of distribution provides up to seven days credit terms, which is popular among buyers. Small and medium companies mostly purchase through importers and wholesalers which have a direct relationship with foreign suppliers. Few wholesalers undertake nation-wide distribution, and almost none carries a complete range of products. The choice of foreign supplier often depends on the retail or wholesale company's ownership, because part of the stock may belong to a foreign investor who may influence decisions based on considerations other than quality or price.

For a new-to-market exporter targeting the Estonian food retail sector, it is advisable to find a professional wholesaler or a local agent with a strategic position in distribution who has the best information about the Estonian market and is able to negotiate and conduct product introduction and promotion. Among the largest food wholesalers are Smarten, ETK, Jungent, Kesko Eesti, Mema Hulgikaubanduse, Hadler, Mobec, LLT, Ovekor, and Haljas.

In the event U.S. exporters cannot sell their goods on credit terms, bonded warehouses provide an attractive option. The status of a bonded warehouse guarantees full maintenance of title to the foreign exporter/supplier. A U.S. exporter with an order from a local importer or wholesaler not able to buy a vessel load may want to bring the product to the

port , put it in a bonded warehouse and sell it in portions over a certain period.

Import and Inspection Procedures

In 1998, Estonia introduced a licensing system for importers of all agricultural and food products with a declared objective to ensure the proper handling of food products and to address consumer concerns over the safety of the imported foods. In 1999, there were 390 licenses issued by the Ministry of Agriculture. Import documentation required by customs authorities includes a copy of the contract, an invoice, a bill of lading indicating the amount, weight and value of goods and the original certificate of origin (form EUR.1 or form A). The 18% value added tax (VAT), the import duty and excise and packaging taxes are collected by customs authorities upon clearance of imported goods at the border, unless the cargo is forwarded to a bonded warehouse. A state fee must be paid for the customs clearance totaling 200 Estonian Kroons (US\$ 15) per customs declaration. Transit through Estonia is free of duty, excise tax, VAT and state fees.

Currently veterinary legislation is being adjusted to EU accession requirements. Imported food and agricultural products need to be cleared and sealed by the border inspection to ensure conformity to legislation applies EU unified import certification of meat and meat products, dairy products and fish. For food imports, a food conformity certificate or producer's declaration and a quality certificate are required.

The Estonian Food Law was implemented in January 2000. It is based on EU directives, and regulates the production, trade and distribution of food products, as well as health issues, consumer protection and food control.

The retail food packages require labels in the Estonian language stating the producer, origin, ingredients, additives, net quantity, importer name and contact information, use instructions, storage conditions and date of minimum durability or the "use by" date. Please consult with the importer regarding packaging and labeling requirements.

Regarding genetically modified (GMO) ingredients Estonia will follow EU regulations and certification requirements. Customer concerns do exist about the presence of GMO ingredients and consumers have shown a distinct interest in organic foods.

The Estonian legal system is presently sufficiently developed to have in place both trademark protection and licensing provisions. There is no specific legal act to regulate franchises yet, and the parties to a franchise agreement are viewed as business partners. Franchising is increasingly being used for business expansion in Estonia.

B. Convenience Stores, Gas Marts, Kiosks

The total grocery product turnover for convenience store, gas marts and kiosks reached about US\$ 372 million in 1999, divided 10/20/10 percent, respectively. This sector's growth is expected to continue at roughly 15% per year. These are chain-store operations. Usually imported products are procured through the local wholesaler. For new-to-market exporters this sector should be targeted in the same manner as described above for supermarkets.

Table: Profiles of Key Companies

Retailer Name	Ownership - (Country)	1999 sales (\$ US Mil)	Number of Outlets	Location: City/Region	Purchasing Agent Type
A Kett	Estonian	11	41	Regional	Wholesaler/ Direct
Edu	Estonian	7	29	Regional	Wholesaler/ Direct
Statoil	Norwegian	3.5	18	Capital/ Regional	Wholesaler
Shell	Dutch	2.5	13	Capital/ Regional	Wholesaler/ Agent
Astri	Estonian	2.5	5	Regional	Wholesaler/ Direct
Neste	Finnish	1.5	12	Capital/ Regional	Wholesaler
Hydro Texaco		0.3	2	Capital/ Regional	Wholesaler

Convenience stores have become increasingly popular and offer a large selection of imported food products. The largest sales are by convenience stores which belong to chains. They are mostly situated in the largest metropolitan areas. Foreign companies are increasing the total number of convenience stores. Traditional independent grocery stores are being converted to convenience stores through franchise or sales agreements. This sector has a stable demand from customers who are willing to pay an extra 10-15% for convenience, high quality, but limited choice. The attractiveness of gas marts may decrease with the fast development of supermarkets with easy parking and increased product varieties.

Kiosks, which were very popular in early nineties, now account for the lowest share of retail food turnover. The recent market entrants with foreign capital are expected to push development through upgrade and consolidation.

The convenience store sector offers some opportunity for sales of food products imported from the U.S.

C. Independent Grocery Stores and Wet Markets

There are a number of traditional markets in the Tallinn metropolitan area, as well as in regional cities. Open markets mostly belong to municipalities and can be widely found in suburbs, regional centers and small towns. Product lines differ greatly by location. In general, they offer a wide range of products at prices which are attractive to low income customers. During the summer, almost all segments of the population prefer shopping at open air markets for fresh domestic produce sold, for the most part, by farmers. Processed vegetables and fruits, confectionary, bread products, dairy products, fish meat and poultry are sold at kiosk-type outlets in traditional markets.

Recent studies by the Estonian Market Research revealed a drop in the popularity of traditional wet markets. Customers have started to shop at groceries and supermarkets as the increasing competition has held down, and even reduced, prices.

This sector offers extremely limited opportunity for sales of imported food products from the U.S. We do not

recommend a marketing strategy aimed at these outlets.

SECTION III. COMPETITION

European food exporters have captured market shares with a strong market presence quality products over the last five-six years as a result of proximity, historical ties, logistic advantages and a service orientation.

Until end of 1999, Estonia's import regime was among the most liberal in the world since no import duties were applied. On January 1, 2000 the Estonian Government put into force its Law on Custom Tariffs, imposing MFN rates on imported goods from third countries which have not entered into free trade agreements with Estonia. Import tariff rates can be found at www.vm.ee/eng/Tollitariifiseadus.htm. The highest MFN duty rates include 25-33% for pork, 48% for poultry meat, 39% for sausages, 10% for chicken legs and wings, 59% for rye, and 40-45% for barley and oats. Such tariff rate changes are a result of Estonia to align its EU requirements.

Because of the newly effective import tariff schedule, exports from European countries faces zero duties, compared to MFN rates for U.S. exports. Given the current trade flows with countries with which Estonia already concluded free trade agreements, these MFN custom tariffs presently apply to about 20% of all agricultural and food imports. Despite tariff increases, there is an opportunity to establish a market for dry, chilled and frozen processed foods. The Estonian food market holds considerable potential for a wide range of competitively priced packaged goods targeted at high/middle income groups and tourists.

In agricultural trade, 1999 imports valued at US\$ 310 million exceeded exports valued US\$ 149 million. Agricultural trade accounted for 10.8% of total imports and 7.5% of total exports. During the early nineties, Estonia was a net exporter of agricultural products. However, agricultural and food imports have surpassed exports since 1995. Main agricultural imports in 1999 were: beverages - soft drinks, wine, beer and liquors (11,3%); meat, meat products and preserves (9.2%); fruits and vegetables (8.2%); coffee, tea and spices (6.3%); preserves of vegetable and fruits (5.9%); food concentrates (5.6%); cereals (5.6%); sugar and sugar confectionary (5.6%) feed grains (4.9%) and dairy products (4.6% of total). Main exports included dairy products, livestock, fish and beverages.

The United States had an agricultural trade surplus with Estonia in 1999, with imports from the U.S. values at US\$ 9.9 million (3.2% of total agricultural imports) exceeding exports valued at US\$ 2.1 million (1.4% of total agricultural exports). This data does not include U.S. poultry exports to Estonia for transshipment to other countries. In 1999, the U.S. was the leading supplier of poultry to Estonia with exports totaling 11.9 thous. MT (65% market share). Other major imports from the U.S. were fish, dried fruits, nuts, oilseeds, vegetable preserves, fruits and vegetables, wines liquors and cigarettes.

In July 2000, Estonia concluded the new European Agreement with the EU Commission. Under the double-zero pact, the EU side has agreed to gradually dismantle barriers to agricultural trade, while EU farm exports to Estonia already enter the country duty free. The Agreement provides for an 80% increase in export quotas for Estonian farm products, and provides an optimistic investment outlook to this market. In 2000, the EU was the main exporter of food products to Estonia, accounting for a 60% market share. Leading EU exports included flour, sugar and cereals.

For most products, domestic production capabilities meet between 70-90% of demand. The table below contains

domestic market value of certain basic food products.

Table: Domestic Market Value and Import Share

Product Groups	Value of Domestic Market, 1999,(US\$ Mil)	Share of Import (5)
Red meat	56	15
Poultry	28	45
Vegetables	48	55
Beverages, incl. Beer	79	40
Chocolate confectionary	17	45
Biscuits	7	65

IV. BEST PRODUCT PROSPECTS

A. Products Present on Market With Good Sales Potential

U.S.-produced products which are available in retail stores and have good market potential include frozen poultry products, rice, pet foods, dried fruits and nuts, wines, liquors, fresh fruits. U.S. products manufactured in other (mainly EU) countries include: chips, soft drinks, packed snacks, confectionary and liqueurs. Concerns exist about the presence of GMO (biotechnology) ingredients and consumers have started to show interest in organic foods.

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

There is an opportunity to establish a market for dry, chilled and frozen processed foods. The product mix should exclude short shelf life products. Low fat, low salt, sugar-free, and cholesterol free products are currently unfamiliar to most consumers.

C. Products Not Present Because They Face Significant Barriers

The recent tariff increase on U.S. product imports disadvantage U.S. sales of the following products which would otherwise have good import potential: snack foods with extended shelf life such as raisins dried foods, nuts, almonds, peanut butter, as well as brown sugar, cake mixes, marshmallows, corn meal, graham crackers, baking chocolate/chips, ice cream mixes, sherbets, wine, frozen foods, pasta preparations, frozen and tinned seafood, frozen and canned vegetables and fruits, maple syrup, as well as assorted convenience goods such as cheese, sauces, salad dressings and breakfast cereals.

V. POST CONTACT AND FURTHER INFORMATION

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Estonian companies data base
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To include your product offers into the Baltics regional "virtual trade fair", check site <http://www.food-fair.com>. You can connect to a business to business database with online catalogs and virtual exhibitions.

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The following publication may prove useful: "US Poultry Export Guide: Poland, Ukraine, Estonia, Latvia" prepared by USDA Agricultural Marketing Service, available at <http://www.ams.usda.gov/tmd/mta/index.htm>

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For more information on exporting U.S. agricultural products to other countries, please visit the Foreign Agricultural Service home page: www.fas.usda.gov and the FAS/Stockholm regional headquarter homepage at www.usemb.se/Agriculture.