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HRI Food Service Sector

Russian HRI Sector Growth Fueled by Rising Incomes

2008

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Report Highlights:

The Russian HRI sector is growing quickly as consumer incomes rise. National restaurant sales are increasing at a rate of 20 to 30 percent annually, and the regional expansion of chain restaurants is driving much of this growth. Many restaurants import the vast majority of their ingredients, creating opportunities for U.S. exports of meat, seafood, wine, and specialty foods. Growing consumer demand and favorable changes in Euro/Dollar and Ruble/Dollar exchange rates are creating even more opportunities for U.S. food and beverage products. Difficulties with customs, port delays, and protectionism all present challenges, but the size and growth of the HRI sector make Russia a valuable market for U.S. producers.

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Executive Summary

The HRI sector is one of the fastest growing segments of the Russian economy, increasing at a rate of 20 to 30 percent per year. There are significant opportunities for American producers to benefit from this boom, as many importers, distributors, and managers in the HRI sector have expressed an interest in buying new products and high-quality ingredients.

Most of the HRI sector's growth is in the fast-food, casual-dining, and coffee-shop segments. The majority of HRI customers are price sensitive, but they are nonetheless interested in new and innovative products. As the Russian restaurant culture grows more sophisticated, the demand for different products increases.

To succeed, American exporters must be prepared to do extensive marketing and to educate potential buyers on how to use their products. Logistics may be a problem, especially as shipping traffic overloads the St. Petersburg port, Russia's primary gateway for American food imports. American products also face substantial competition from Western Europe, Asia, and South America.

While the main markets for American products are still in Moscow and St. Petersburg, the HRI sector is rapidly developing in other large cities. These include Nizhniy Novgorod, Yekaterinburg, Kazan, Novosibirsk, and tourist cities on the Black Sea such as Sochi, the site of the 2014 Olympic Games. Operating outside major regions, however, adds an additional layer of logistical complication for American exporters. To overcome these difficulties, they will need to collaborate with strong importers or distributors.

SECTION I: MARKET SUMMARY

Russia has one of the fastest growing economies in the world. Its real GDP growth rate was 8.1 percent in 2007 and 7.4 percent in 2006. The HRI sector is growing even faster, at a rate of 23 to 26 percent annually. Consumer income rose 10.4 percent in 2007 after having grown 13.3 percent in 2006. In 2007 consumer demand rose 15.2 percent over the 2006 level. Russians now spend more of their income on food than any other country in Europe, and dining out is beginning to replace the home as the preferred venue for entertaining.

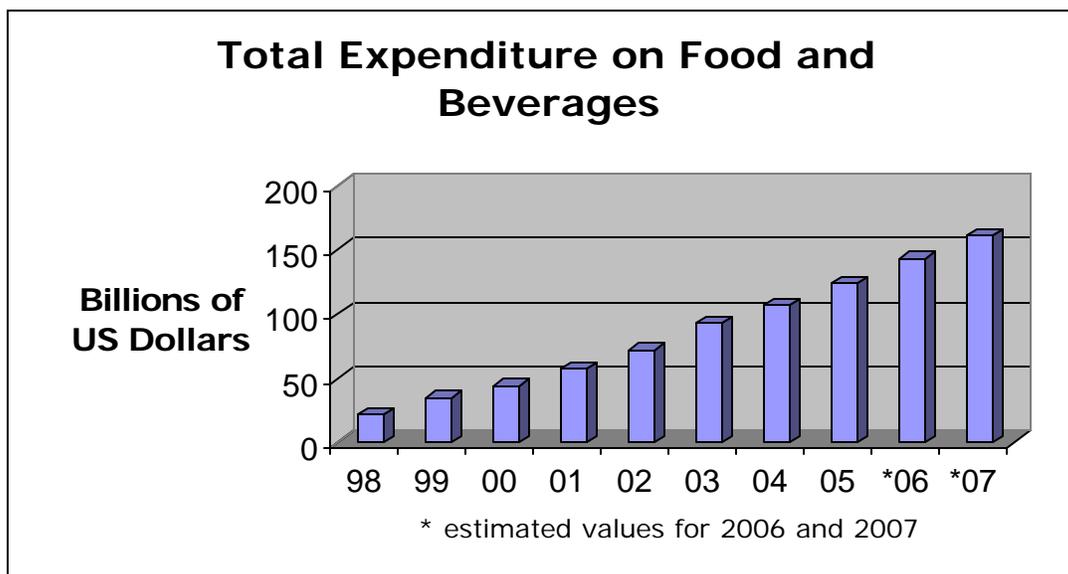
The number of restaurants and hotels in Russia lags behind that in other countries. In the mid-1990's new restaurants first opened in Moscow and St. Petersburg. Since then, there has been a shift in people's outlook, and dining out is becoming the norm rather than a special occasion. Restaurants are appearing in suburbs and smaller cities across Russia and the development of modern shopping malls, hypermarkets, trade venues, and entertainment centers has helped leading foodservice operators enter regional markets more easily.

Socio-demographic factors, including urban growth and the entry of more women into the workplace, have led increasing numbers of people to eat their main meals in restaurants. More people are dining out for lunch, and business lunches are standard in many mid-range restaurants. People are also increasingly health conscious, and the younger generation often looks for low-calorie options. As a result, in 2006 the leading fast-food operator, McDonald's, began including calorie information on its packaging in Russia. Other fast-food restaurants and cafes report increased sales of healthy menu-offerings.

Russian consumers are also traveling abroad more often. Travel exposes them to a wide variety of tastes and foods that they subsequently wish to find at home. Russians have discovered a variety of cuisines such as Italian, Japanese, and American in addition to long-familiar Georgian and Central Asian culinary traditions. Russian menus are quite diverse, and consumers tend to order multiple courses even in fast-food restaurants and coffee shops.

Russians are also spending more on alcohol, but they are moving away from the traditional vodka. Beer and wine are becoming increasingly popular, as are fashionable drinks such as whisky, cognac, and brandy. Cocktail drinks have also become fashionable and customers are increasingly ordering spirits by brand name. Figure 1 shows the overall increase in spending on food and beverages.

Figure 1. Russia: Food and Beverage Spending



Source: Euromonitor

HRI Sub-Sectors

Restaurants

The Russian restaurant market has grown considerably in the past few years. According to Russia's State Statistics Bureau (Rosstat), the volume of the restaurant industry in Russia reached \$14.6 billion in 2006, of which \$3.52 billion was located in Moscow.

The restaurant market grows annually at a rate of about 20 percent per year nationwide. The Moscow market is the fastest growing, increasing annually by 25 to 30 percent, while other regional markets have annual growth rates between 12 and 15 percent. The high tempo of growth seems to be tracking along with rising household incomes and "restaurant culture" is advancing in Russia as a regular part of social and business activities. Since 2003, consumers' "away-from-home" food expenditure as a share of total consumer expenditures has grown annually by 3 to 4 percent.

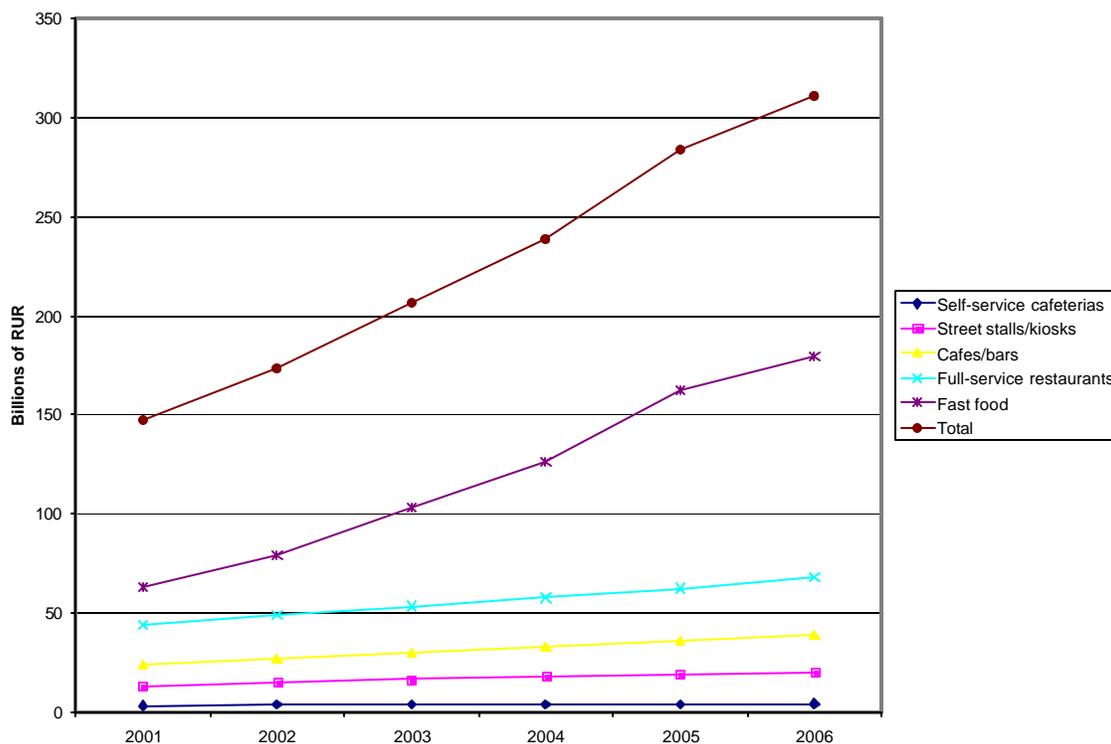
The number of cafes, restaurants, and other food outlets in Russia totals about 30,000. Although Moscow and St. Petersburg are still by far the largest restaurant cities in Russia, leading foodservice operators have begun regional expansion into other wealthy cities. The markets of Moscow and St. Petersburg are expected to reach saturation in the near future, so modern retail formats such as shopping malls, business centers, and entertainment hubs play a significant role in regional expansion of foodservice competitors.

The Russian restaurant market consists of several market niches, each of which is different in terms of total food sales, number of players, and growth rate:

- Fine-Dining/Full-Service Restaurants: higher priced/exclusive outlets;
- Casual-Dining restaurants: affordable, family dining outlets;¹
- Fast-food, which is divided into two separate segments: Stationary fast-food and street/mobile fast-food (kiosks, stalls, etc.); and
- Coffee shops.

Fast-food outlets, casual restaurants, and coffee houses are currently the most popular and fastest-growing sectors in Russia. Figure 2 and Table 1 show the growth of restaurant sales by sector.

Figure 2. Russia: Restaurant Sales by Sub-Category



¹ “Democratic” in this peculiarly Russian sense means affordable, and refers to the casual-dining market segment.

Table 1. Russia: Restaurant Sales by Sub-Category

RUR, billion	2001	2002	2003	2004	2005	2006
Cafes/bars	23.5	27	30	33	35.7	38.8
Fast-food	63.4	78.7	103	126.2	162.7	179.6
Self-service cafeterias	3.3	3.5	3.7	3.8	4	4.3
Street stalls/kiosks	13.3	15.3	16.5	17.9	19.2	20.3
Full-service restaurants	43.7	48.9	53.5	57.6	62.4	67.8
Total	147.2	173.4	206.7	238.5	284	310.8

Source: Euromonitor

Three main segments of the market stand out clearly. The highest-priced segment, “fine-dining” in Western terminology, has an average check of more than \$70 per person. Patrons receive refined cuisine, unique design, good service, and the availability of private dining space. The lowest-priced segment, fast-food, mainly consists of chains such as McDonald’s, Rostik’s-KFC, and Kroshka-Kartoshka. The medium-priced or casual segment has an average check of \$20 to \$70 per person, and it includes chains such as Il Patio, Yolki-Palki, Goodman, and Planet Sushi. The medium-priced segment has achieved a high growth rate by successfully combining the advantages of the other two: quality cuisine and service at affordable prices.

Chain and franchised restaurants are no longer the exception in Russia, especially in Moscow and St. Petersburg where the food service market is more developed. More restaurateurs are recognizing the advantages of developing chains due to the higher popularity and profitability of such outlets. Chain operators have a strong market position, holding an increasing value share of Moscow restaurants. Today, foodservice chains comprises about 31 percent of the market. While it is clear that a restaurant chain has more money and more clients, a stand-alone restaurant is not necessarily less profitable. Table 2 shows the number of Russia’s independent and chain outlets in 2006.

The self-service cafeteria was the main foodservice format during the Soviet period, and most self-service outlets are currently concentrated in institutional catering. Institutional self-service cafeterias usually operate with the financial support of an institution and offer lower-quality food and services. Consequently, many clients are switching to other foodservice formats such as fast-food and cafés/bars.

According to analysts’ predictions, the market will continue to grow for at least another five years. The market potential for Russia’s restaurants is enormous. The average public outlet in the U.S. caters to 150 people per day. In Europe, that figure grows to 300, and in Russia, it reaches 2000.

Table 2. Russia: Consumer Foodservice by Independent versus Chain Outlets (2006)

Outlets	Independent	Chained	Total	% of Total
Consumer foodservice	45,340	8,651	53,991	100
Cafés/bars	8,235	1,337	9,572	17
Full-service restaurants	5,939	1,517	7,456	12
Fast-food	15,346	4,047	19,393	35
100% home delivery/takeaway	430	135	565	1
Self-service cafeterias	2,030	50	2,080	4
Street stalls/kiosks	13,360	1,565	14,925	26
Pizza consumer foodservice	2,809	600	3,409	5

Source: Official statistics, trade associations, trade press, company research, trade interviews, and Euromonitor International estimates

Moscow's Restaurant Market

In 2007, Moscow is the largest city in Europe with a population of 10.47 million (according to official statistics)². While Moscow has only 9 percent of Russia's population, it generates 20 percent of Russia's gross domestic product. With 8,000 restaurants excluding office cafeterias, Moscow is Russia's largest restaurant market. Direct Contact Group, a market research firm, conducted a study that estimates consumers spent \$3.52 billion in 2006 in Moscow restaurants. Casual-dining restaurants generated \$1.8 billion, quick-service restaurants \$780 million, fine-dining restaurants \$340 million, coffee shops \$180 million, and fast-food restaurants including bars, canteens, and self-service snack bars \$420 million.

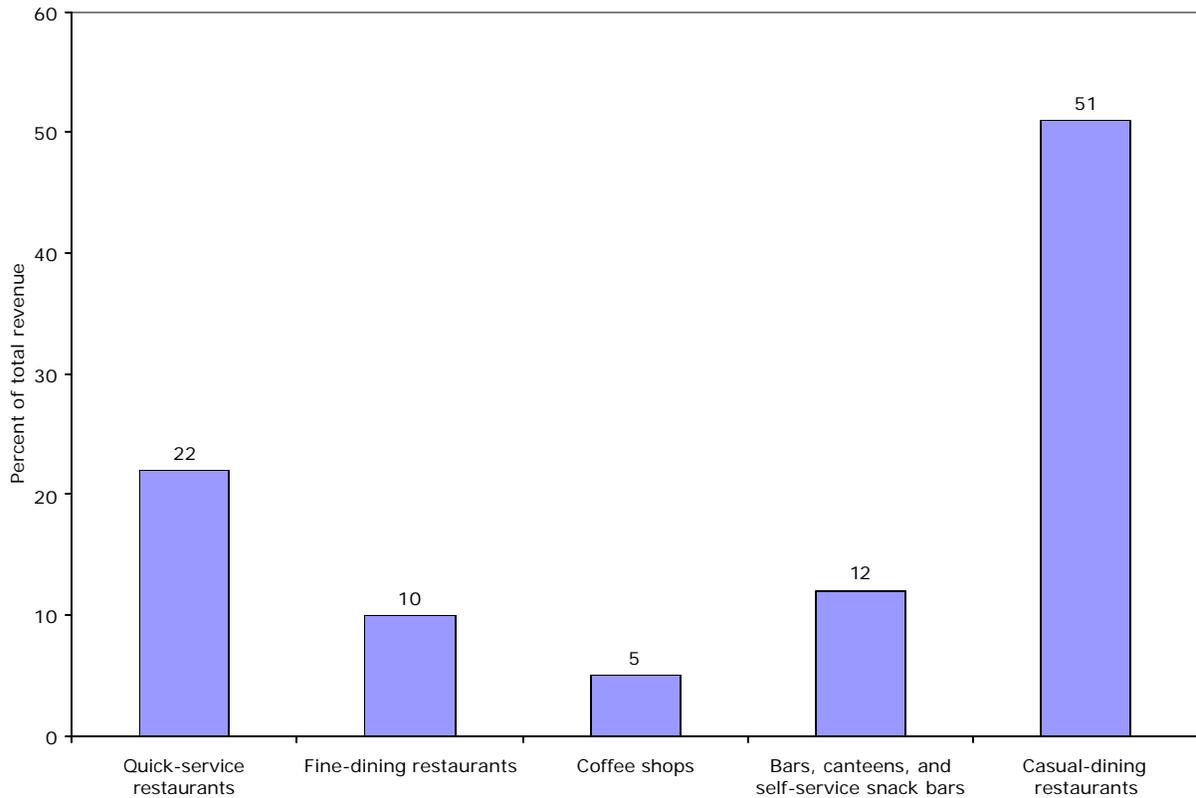
The DISCOVERY Research Group forecasts that the value of Russia's restaurant industry will reach 630 billion rubles (\$27 billion) in 2009, with 120 billion rubles (\$5.15 billion) in Moscow. Nevertheless, Moscow's restaurant market is far from saturated when compared to the number of food outlets per 100,000 inhabitants in other major cities throughout the world.

Coffee shops and casual-dining restaurants saw the most active profit growth in 2006, with profits rising 38 percent and 32 percent respectively. Profit growth in the fast-food sector was 26 percent. Chains are also gradually replacing independent restaurants.

In 2006, the total number of Moscow restaurants grew by 11 percent, while total revenue grew by 16 percent. About 4.8 million people regularly visited the city's restaurants excluding office cafeterias. This audience gradually increases by about 3 to 5 percent annually as incomes rise. Figure 3 show's restaurant revenue by sub-category.

² It is estimated that Moscow's population approaches 15 million when unregistered and illegal residents are included.

Figure 3. Russia: Revenue by Sub-Category, Moscow 2006



Source: Industry data

Major Restaurant Operators in Russia

According to Formen Consulting, a consumer and market research company, there are currently 25 to 35 restaurant chains operating in Russia, each of which manages between 20 to 250 outlets. McDonald’s, Rosinter Restaurant Holding, Arkadiy Novikov Restaurants, and Coffee House are the largest restaurant chains in Russia. Table 3 shows the brands, types, and number of outlets of Russia’s largest restaurant chains.

Table 3. Russia: Large Chain Restaurants

Holding Company	Brands	Type	# Outlets March 2008
Rosinter	Planet Sushi	Casual (Asian)	79
	Il Patio	Casual (Italian)	90
	T.G.I. Friday's	Casual (American)	20
	American Bar & Grill	Casual (American)	5
	Sibirskaya Korona	Casual (beer-restaurant)	14
	Coffee houses and fine-dining restaurants		
Rostik's-KFC	Rostik's-KFC	Fast-food	141
McDonald's	McDonald's	Fast-food, and coffee houses	190
	McCafe		
Novikov Group	Different concept restaurants	Fine-dining	30
Alfa Capital Partners	Yolki - Palki	Casual (Russian)	60
	Malenkaya Yaponiya	Casual (Asian)	6
Coffee House	Coffee house	Coffee house	200
	Asia café	Casual (Asian)	14
GMP Planet Gostepriimstva	Sbarro	Casual (Italian)	114
	Vostochnyy bazar	Casual (Asian)	31
	Viadzhio	Casual (Italian)	7
Restaurants Association Vesta Center International	Yakitoriya	Casual (Asian)	53
	Gi-No Taki	Casual (Asian)	6
RP-Com	Goodman	Casual (steakhouse)	8
	Filimonova & Yankel	Casual (fish-house)	3
	Kolbasoff	Casual (beer-restaurant)	8
	Mamina Pasta	Casual (Italian)	2

Source: Official statistics, trade associations, trade press, company research

McDonald's, the largest chain of fast-food restaurants in the world, entered Russia in 1990 and opened its first restaurant in the center of Moscow. Currently, 196 McDonald's restaurants, including 34 McCafes, operate throughout Russia and serve 200 million

customers annually. There are 80 McDonald's restaurants in Moscow and 35 in St. Petersburg. The company operates in 29 Russian cities.

All McDonald's restaurants operating in Russia are corporate facilities rather than franchises. McDonald's Russian business model contrasts with the model used in the U.S. and Europe, where franchisees run 80 percent and 50 percent of McDonald's restaurants respectively.

McDonald's operates in 113 countries, and Russia is one of the ten top countries by sales volume. McDonald's growth rate in Russia is between 20 to 30 percent annually. The fast-food giant plans to open 36 new restaurants in Russia by the end of 2008. The company spends between \$1.5 million to \$2 million to set up each new restaurant. Opening one cafe costs about \$250,000. McDonald's opened 21 outlets in 2007 and 23 restaurants in 2006.

McDonald's also plans to expand its McCafe chain, its premium class coffeehouse format. The first McCafe opened in Russia in 2002 and now there are currently 34, 17 of which are in Moscow and 10 in St. Petersburg. McCafe also operates in Yaroslavl, Nizhniy Novgorod, Yekaterinburg, Volgograd, Kazan, and Ufa.

The corporation also owns the McComplex food processing plant and distribution center in the Moscow region. It has invested \$45 million in the McComplex.

Rosinter Restaurants Holding (Rosinter) is a major player on the Russian restaurant market. Its market share, according to the Renaissance Capital research group, was 8.5 percent in 2007. The company gained its leadership role by its early deployment of chain restaurants in the upper/middle-priced segment of the market where Rosinter ownership is 17 percent. As of June 30, 2008, the holding company operated 262 outlets, including 67 franchised restaurants in 29 cities in Russia, the CIS, Central Europe, and the Baltic states. The company offers Italian, Japanese, American, and Russian cuisine under its proprietary brands (Il Patio, Planet Sushi, and 1-2-3 Cafe) and its licensed brands (T.G.I. Friday's and Sibirskaya Korona).

Rosinter created a strategic alliance with the American Yum!Brands, and it opened a chain of fast-food restaurants under the Rostik's-KFC brand in 2006. In a joint venture with Whitbread PLC, the company is currently developing the Costa Coffee chain in Russia.

In May 2007, Rosinter Restaurants Holding held its IPO and offered 26 percent of its shares at the price of \$32 per share. The move attracted \$100 million and fixed the market value of the company at \$384 million. Rosinter reported consolidated revenues of \$268.2 million in 2007.

The company holds three main objectives. The first is to accelerate the expansion of its coverage in Russia, the CIS, and Europe. The second is to increase its presence in transportation facilities, trade centers, and Moscow residential areas. The third is to develop new formats of its brands for high-traffic locations. In 2008, Rosinter plans to open 90 outlets, including 27 franchised restaurants.

Arkadiy Novikov Restaurant Group (Novikov Group) includes nearly 45 restaurant-retail-entertainment projects of various formats and price ranges. The company has launched and managed restaurants since 1992. The Novikov Group is slightly less chain-oriented. It operates more than 30 different Moscow high-end concept restaurants, along with a few restaurant chains such as Yolki-Palki, Malenkaya Yaponiya, Kish-Mish, and Sushi Vesla. 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. The Novikov Restaurant Group's consolidated revenue was \$180 million in 2006.

Six months ago, the rapidly growing mid-priced restaurant chain Yolki-Palki, which specializes in traditional Russian cuisine, attracted the interest of the portfolio investor Alfa Capital Partners. The alliance now concentrates on developing the current brands Yolki-Palki and Malenkaya Yaponiya, which specializes in Japanese cuisine. The Yolki-Palki chain, established in 1996, currently operates 47 restaurants of both Yolki-Palki and Malenkaya Yaponiya, nine of which opened last year.

RP-Com (Restaurant Professional Company) is one of the top 10 foodservice operators in Moscow. RP-Com currently owns the following restaurants in Moscow: eight Goodman steakhouses, three Filimonova & Yankel fish-houses, eight Kolbasoff beer-restaurants, the French café Le Gâteau, and three Italian Mamina Pasta restaurants. While RP-Com is not the leader in any one foodservice format, the company's future growth seems promising because it has built a reputation on quality and service. During its five years of foodservice experience, the company has gained success in the niche of North American full-service 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 third largest chain of North American full-service restaurants in Moscow as well as in the whole of Russia. The company is planning significant expansion beyond the capital city, including plans to open Goodman's steakhouses in each city in Russia and the CIS with a population of one million or more.

Table 4 shows the revenue of Russia's largest restaurant chains.

Table 4. Russia: Revenue of Restaurant Chains, \$ million

Holding Company	2004	2005	2006	2007 (plan)
McDonald's	~ 550	~ 700	840	
Rostik Group	146	188.3*	305**	
Novikov Group	81.9	94.9	180	
Coffee House		~ 50	90	
Restaurants Association Vesta Center International			70-80	
Kroshka-Kartoshka	~ 20	39	58	85-90
Shokoladnitsa	13	25	57	
GMP Planet Gostepriimstva	~ 40	~ 60	over 50	over 100
RP-Com	9	35	~ 40	70

Source: Restaurator Magazine, trade press

* This is Rosinter's revenue. The consolidated sales of the Rostik Group in 2005 were \$235 million.

** Rosinter's revenue was \$205 million, while Rostik's-KFC's revenue was over \$100 million.

Fine-Dining/Full-Service Restaurants

Haute cuisine appeared in Russia in the mid 1990's, and there is no shortage of high-end restaurants with extravagantly expensive checks in Moscow and St. Petersburg. Fine-dining restaurants are associated with names such as Arkadiy Novikov and Andrey Delos, 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, high-end wines, and spirits.

Casual-Dining Restaurants

Casual dining is one of the fastest-growing segments of the restaurant market, with growth rates between 15 to 25 percent annually. The leading position in this segment belongs to the chain operators, including those specializing in Russian, North American, Italian, and Asian cuisine. The value growth rate of full-service chain restaurants increased significantly from 11 percent in 2001 to 27 percent in 2006. Moreover, the leading chains occupied 36 percent of total full-service chain restaurant sales in 2006. The poor development of independent operators across most full-service restaurant formats decreased the number of non-chained casual restaurants, 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. Even though Russian consumers are becoming wealthier, most of them are not willing to visit high-priced foodservice outlets on a regular basis. They prefer a diverse menu at democratic prices. The average price for a meal at one of these restaurants ranges from \$20 to \$70 per person.

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 costs 15 to 20 percent more than opening a regular 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. Another added expense is the marketing and education necessary to promote steakhouse culture.

Currently, the main American-cuisine restaurants in Moscow are T.G.I. Friday's and the American Bar & Grill chains (operated by Rosinter), Goodman steakhouses (operated by RP-Com), and three Torro Grill and Wine Bars. Even though the number of steakhouses is growing slowly, overall consumption of steaks is increasing steadily. These restaurants use imported meat, usually from Australia or the U.S., since local suppliers do not provide consistent quality.

The enormous popularity of Japanese cuisine made Asian full-service restaurant chains the most dynamic category of casual restaurants in 2006, with value growth rate of 25 percent. Japanese restaurants, with sushi and fish menus, strongly represent the fish and seafood concept restaurants in Russia. As Russian consumers become increasingly health conscious, sushi's image as a healthy food is an essential component of this growth.

Very few casual chain restaurants have a centralized system of purchasing. Most decisions regarding products and purchasing are made at the restaurant 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.

According to industry experts, casual eateries use imported meat, seafood, desserts, seasonings, and a variety of ingredients. While quality is of some concern, prices dominate purchasing decisions. American products will need to be cost-competitive to attract business in this segment.

Fast-Food

The fastest-growing restaurant category in Russia is the fast-food sector with an annual growth rate of 25 to 30 percent from 2004 to 2007. According to restaurant consulting group RestCon, Russia's fast-food market was worth \$1.5 billion in 2006, including \$640 million in Moscow alone. Experts predict that the fast-food and street-food market will not reach saturation until 2014 to 2016.

McDonald's, Rostik's-KFC, and Sbarro chains together occupied 36 percent of fast-food chain sales in 2006. McDonald's remained the absolute leader with a 30 percent value share of fast-food chain sales. McDonald's' experience has become a "how-to manual" for leading Russian fast-food operators. From McDonald's, they learned how to create a system of quality control and standardized foodservice technologies. Table 5 shows the market shares of fast-food chain operators.

Table 5. Russia: Market Shares of Fast-Food Chain Operators

Company	Global Brand Owner	2003	2004	2005	2006
McDonald's	McDonald's Corp	35.3	30	30.7	30.3
Rostik's	Rostik's International Inc	3.6	5	5.9	4.3
Sbarro	Sbarro Inc	2.8	2.9	3	3
Rostik's-KFC	Rostik's International Inc				2.8
Teremok	Teremok - Russkie Bliny		0.4	0.6	1.4
Kroshka-Kartoshka	Tekhnologiya & Pitanie Ltd	0.4	0.6	1	1.4
Chaynaya Lozhka	Solo OOO	0.5	1.2	1.3	1.4
Baskin-Robbins	Dunkin' Brands Inc				1.3
Others		57.4	56.9	57.5	54.1
Total, %		100	100	100	100

Source: Official statistics, trade associations, trade press, company research, trade interviews, Euromonitor International estimates

The food-court format is gaining popularity among fast-food operators. The most dynamic chains - including Rostick's-KFC, Chaynaya Lozhka, Sbarro, and Baskin-Robbins - have opened numerous outlets in shopping malls and hypermarkets.

Russian consumers are growing fond of the simple menus, good-quality food, and affordable prices offered by fast-food outlets. Consequently, more Russians are visiting fast-food outlets

on a regular basis. According to an online inquiry by Online Market Intelligence, 91 percent of Moscow and 93 percent of St. Petersburg consumers frequented a fast-food restaurant in 2007. Pancakes, burgers, chicken, pizza, and baked potatoes are the most popular types of fast-food in Russia.

Americans often move quickly through food courts, stopping for a quick bite while shopping. Russians, however, usually visit food courts to socialize. In Russia, the food court is a popular venue for young people to spend time together. 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 Krosha-Kartoshka (potato stand), Stardog!s (hot dogs), and Teremok (Russian crepes) are ubiquitous throughout the major cities and are expanding regionally as well. Table 6 shows the growth of different restaurant chains in Russia.

Table 6. Russia: Fast-food and Free Flow Chains

Chain Name	Country of Origin	Year est. in Russia	Number of Outlets			
			2005	2006	2007	March, 2008
Kroshka-Kartoshka	Russia (Moscow)	1991	141	170	230	252
Stardog!s	Russia (Moscow)	1993 (2003 new brand)	186	197	224	234
McDonald's	USA (Canada)	1990	137	157	174	190
Baskin Robbins	USA	1992	118	132	139	139
Teremok	Russia	1998	62	92	135	142
Rostik's - KFC	Russia/USA	1993 (2005 new brand)	87	97	135	141
Sbarro	USA	1997	52	83	111	114
Riksha I Van	Russia (Moscow)	1998 (2006 new brand)			79	90
Chaynaya Lozhka	Russia (St.Petersburg)	2001	28	42	59	64
Eurasia	Russia (St.Petersburg)	2001	30	49	49	49
Moo - moo	Russia (Moscow)	2000		14	17	17
PrimeStar	Russia/USA	2007			13	14
Grabli	Russia (Moscow)	2003	1	3	4	5

Source: Restaurator Magazine, trade press

Fast-food restaurants tend to use a higher percentage of local ingredients (around 50 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 created McComplex to produce nearly 56,000 hamburger patties daily, but McComplex cannot produce enough to meet its needs. The company therefore buys additional hamburger from meat suppliers.

Produce, dairy, and egg products are usually sourced locally, but import opportunities do exist. Many chains use imported sauces and ingredients. Smaller fast-food restaurants that do not have the capital or scale to justify creating their own production facilities may also import meat and produce. Poultry and beef are the leading imported meats in this category. Most of the larger international chains have an internal distribution network, while some independent and smaller chains rely on traditional or specialty distributors. Fast-food is an increasingly attractive market for overseas investors and the appearance of new fast-food players in Russia is not surprising. Experts explain the active interest of global restaurant chains in the Russian fast-food market by its high, steady annual growth rate.

CKE Restaurants, a major U.S. fast-food company, sold its franchise for Carl's Junior, its main brand, to St. Petersburg-based Yarkaya Zvezda in 2005. The franchise is estimated to have sold for \$300,000 to \$500,000 plus a royalty ranging from 1.5 to 2 percent of the chain's future turnover. The agreement stipulates that by 2013, Yarkaya Zvezda will operate no fewer than 50 Carl's Junior restaurants in Russia. In September 2007, Yarkaya Zvezda opened its fifth premium fast-food restaurant in St. Petersburg, and it plans to enter the Moscow market in 2008.

Church's Chicken, the American fried-chicken restaurant chain, opened its first Texas Chicken restaurants in Moscow and St. Petersburg in 2007 through its franchise European Active Corp. It plans to open up to 30 restaurants in Russia over the next three years. Church's main competitor is KFC, operating as Rostik's-KFC in Russia. In March 2008, KFC operated 141 restaurants in Russia, and it plans to open 300 more by 2010.

Quick, a Belgian fast-food restaurant, signed an agreement in July 2007 with Russian Tashir Group to invest about \$100 million to build 80 restaurants over five years. Quick is a competitor for McDonald's. Quick Russia will create three market lines, opening restaurants in shopping-center food-courts, street retail, and drive-ins. Quick Russia opened its first restaurants in Moscow and Tula shopping centers in April and in Kaluga and Yaroslavl in May 2008.

Coffee Houses

Today, Russia's coffee-shop market is one of the most dynamic segments of the HRI sector with profits of 30 percent. The Russian State Statistics Committee (Rosstat) estimates that there are approximately 1,000 coffee shops in Russia with revenues of about \$400 million. Specialized coffee shops chains continue to demonstrate the highest rate of value growth, reaching 45 percent in 2006.

Coffee shops have become increasingly popular over the past several years among urban consumers in the largest Russian cities. They view coffee houses as the most convenient place for socializing, while most provincial citizens still prefer tea and pay visits to each other's homes.

Currently, coffee-shop chains are highly prevalent in Moscow and St. Petersburg. There is an increasingly high concentration of the leading chains, including Coffee House, Shokoladnitsa, Moka-Loka, McCafé, and Idealnaya Chashka. Non-chain coffee shops are significantly less common. Industry analysts have begun to forecast saturation, so leading operators are increasing investment in regional expansion. Rapid development of modern hypermarkets, trade centers, shopping malls, and business centers helps leading operators, more so than independent ones, to enter regional markets. Coffee shop-chains increased their value share of total cafés from 8 percent in 2001 to 22 percent in 2006.

Two leading coffee-shop chains, Coffee House and Shokoladnitsa, together opened 146 new outlets in 2007. Most of these are located in the food courts of new shopping malls and business centers. Large companies in the market benefit from placing their outlets in shopping centers that attract a large number of visitors. Highly profitable coffee shops continue to attract new customers, and new local chains such as Kofejnya No 7 in Ekaterinburg, Traveler's Coffee in Novosibirsk, and Pitjcofe in Rostov-on-Don have strengthened their competitive positions in local markets.

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 and, as of July 2008, operates 6 coffee shops in the capital. Following Starbucks, Whitbread and Rosinter Restaurants Holding "Rosinter" signed a joint-venture agreement and announced their intention to launch the Costa Coffee chain in Russia. According to the contract between Whitbread and Rosinter, more than 200 Costa stores will open in the next five years. They will concentrate on Moscow and St. Petersburg during the first year, expanding to other Russian regions thereafter. In the near future, the leading restaurant chain in Russia, Rosinter, will rename its Moka-Loka coffee chain as Costa Coffee. The appearance of these leading multinational coffee chains on the Russian market may change the situation of the coffee-shop segment. Table 7 shows the growth of Russia's coffee-shop chains.

Table 7. Russia: Coffee-Shop Chains

Chain Name	Number of Outlets				Locations	First Year of Operation
	2005	2006	2007	March, 2008		
Coffee - House	81	115	180	200	Moscow, St.Petersburg, regions	1999
Shokoladnitsa	35	74	155	158	Moscow, St.Petersburg, regions	2001
Moka - Loka	22	21	16	16	Moscow, St.Petersburg, regions	2002
Idealnaya Chashka			13	13	St.Petersburg, Moscow, regions	2000
Coffee - Mania			11	11	Moscow	2001
Coffee Bean	4	5	8	8	Moscow, regions	1996
Starbucks			2	2	Moscow	2007
Costa Coffee				1	Moscow	2008

Source: Restaurator Magazine, trade press

The Russian coffee-shop format differs from Western standards, because Russian consumers require a larger assortment to satisfy their eating patterns. According to industry sources, coffee accounts for 80 percent of sales for Idealnaya Chashka and Coffee Bean, but only 40 percent of those for Coffee House and 15 percent for Shokoladnitsa. Coffee shops in Russia constantly increase their non-coffee selections to include alcoholic drinks, dairy cocktails, salads, hot dishes, desserts, and tea. The average bill at one of these coffee shops is between \$15 and \$25, and drinks average only 30 to 40 percent of the total check.

Russian coffee shops that sell a variety of desserts and confectionery products have created a new market for U.S. exporters of nuts, fructose, marzipan, and dried fruit.

The rise of chained coffee shops has boosted consumer interest in specialty coffees such as cappuccino and flavored coffee. This trend has created a growing demand for Ready to Drink (RTD) coffee. RTD coffee gained a Russian presence in 2003. It is regarded as a fashionable western drink and has proven particularly popular among urban consumers in the larger cities. RTD coffee, especially with milk, is another interesting market for U.S. exporters.

Hotels

According to Russia's State Statistics Bureau (Rosstat), Russia had approximately 4000 functioning hotels able to accommodate about 354,000 guests at the end of 2006. Almost 17 percent of hotel rooms are in Moscow, 13 percent are in Russia's popular Black Sea resort area Sochi, and 9 percent are in St. Petersburg.

Russia's hotel industry is facing a severe room shortage. Jones Lang LaSalle and Colliers International, the real estate money management and services firms, estimate that there are currently only 14,000 Western business-style hotel rooms available. In fact, most existing four and five-star hotels in Moscow and St. Petersburg were built during the last decade. As a result, Moscow currently has just 8,000 Western business-style hotel rooms, and St. Petersburg has only 3,000. This pales in comparison to other European capitals. For example, London and Paris each have 100,000 such rooms. Other large cities in Russia often have few lodging options other than old Soviet-style hotels. Given the increase in tourism in recent years, the surge in demand for hotels and other types of accommodation is causing major problems in Moscow, St. Petersburg, and almost all other regional centers. Moscow alone hosts about 4.5 million tourists every year, with St. Petersburg close behind. In contrast, Vienna attracts 3 million and Berlin attracts 3.2 million. Due to its close proximity to Europe, St. Petersburg attracts most of the international business travel. The current average occupancy rate in Moscow is an estimated 73 percent overall, rising to around 80 or 90 percent in the three-star hotel segment. There is an estimated shortage of 10,000 rooms every year. Table 8 shows the available rooms by category in Moscow and St. Petersburg in 2007.

Table 8. Russia: Available Rooms in Moscow and St. Petersburg by Category, 2007

Star Rating	Moscow	St. Petersburg
5	8%	9%
4	16%	20%
3	43%	50%
2	28%	7%
Small hotels	5%	14%
Total	100%	100%

Source: Becar Commercial Property Moscow and St. Petersburg municipal government

Accommodation costs, high by international standards, are a symptom of the room shortage. Table 9 shows the increase in accommodation costs over time. Room prices have risen from 20 to 40 percent per year since 2000, and a typical room in a Western hotel now costs more than \$300 dollar per night. While these prices are good for hotel operators' profits, the lack of good affordable accommodation reduces Russia's tourism potential, particularly for business travel. Other sectors such as restaurants and theaters could grow even faster if there were higher tourist capacity.

Table 9. Russia: Accommodation Costs in Moscow Hotels (\$/per double room/per night)

Star rating	2004		2005		% change 2005/2004	2006		% change 2006/2005
	Price range	Mean price	Price range	Mean price		Price range	Mean price	
5	330-439	398	413-750	554	+39	445-1000	720	+30
4	115-348	246	140-566	332	+34.9	150-650	400	+20.5
3	60-186	123	76-255	149	+21.1	100-275	188	+25.8
2	45-57	50	53-67	61	+22	65-80	73	+19.7

Hotels, however, take time to develop. The bureaucratic requirements to operate a hotel have slowed the pace of development for large internationally managed hotels. Most internationally branded hotels are operated as franchises rather than under the direct control of the home office. Business tourism makes up a substantial share of the market, with almost 2 million international visitors per year on top of domestic business travelers. Business travel has steadily increased without showing the same seasonal fluctuations of tourism. The number of business travelers in Russia is forecast to grow 300 percent by 2015. Table 10 describes Russia's five and four-star international hotels.

Regions outside of Moscow and St. Petersburg represent a small fraction of the tourist industry, but some areas such as Sochi and Vladivostok are growing quickly. Yekaterinburg, Novosibirsk, Nizhny Novgorod, Krasnoyarsk, Kaliningrad, and Kazan are other regions where tourism is growing, particularly for business travel. Major hotel chains are opening facilities in these regions, and the Radisson just opened a 160-room Park Inn Hotel in Yekaterinburg.

As many experts predicted, the 2014 Sochi Winter Olympic Games is spurring hotel development in the region. All in all, 390 new hotels are expected to be built across Russia by 2010, with many in Moscow and several in major regional capitals. International hotel operators are building hotels before upcoming events in the Russian regional centers. The following events are planned for the near future: the Shanghai Cooperation Organization Summit in Yekaterinburg in 2009, the APEC Summit in Vladivostok in 2011, the World Students Games in Kazan in 2013, and the Sochi Winter Olympic Games in 2014. Hyatt and Marriott will soon open hotels in Yekaterinburg, while Accor Group and Marriott will open hotels in Vladivostok by 2011.

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.

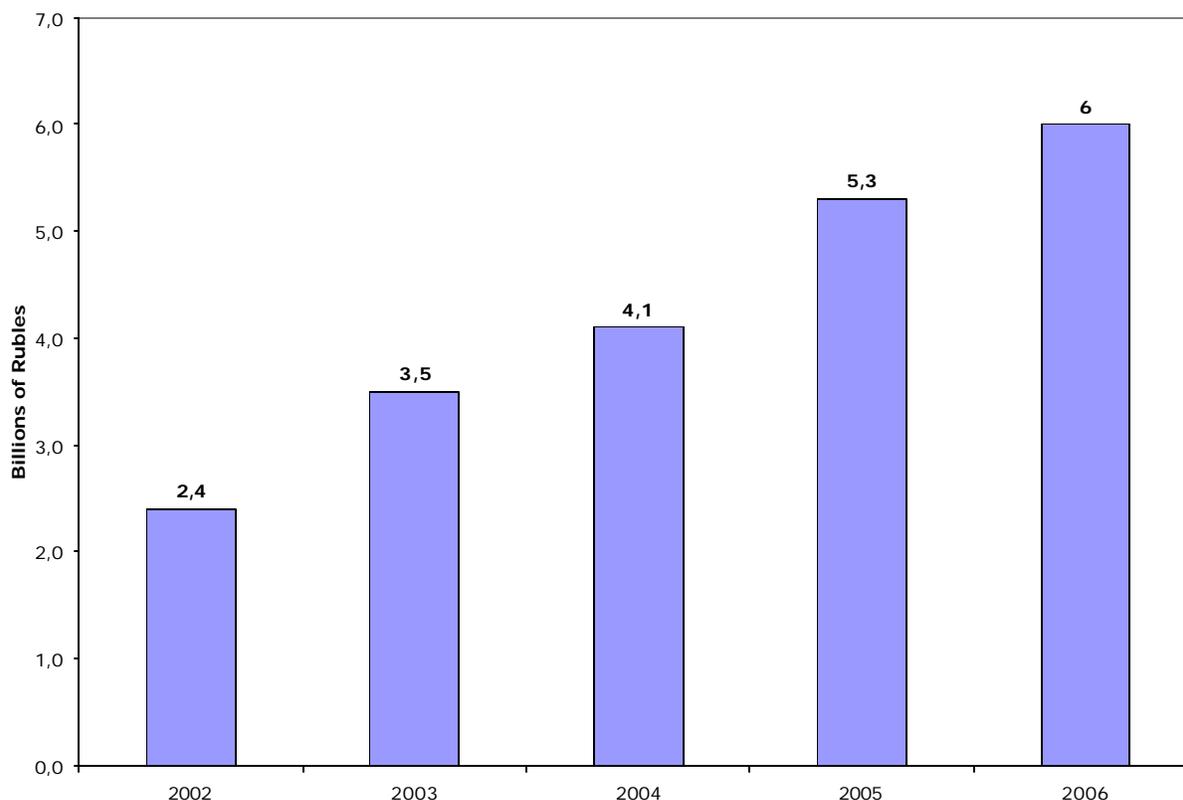
Table 10. Russia: Five and Four-Star Hotels Managed by International Corporations

Hotel Operator	Moscow Hotel Name	# of Rooms	Other Locations	Planned Expansion
Raffles	Swissotel Krasnye Holmy 5*	233		
Marriott International	Renaissance Moscow Hotel 4*	475	Samara	Vladivostok
	Courtyard Moscow City Center 4*	218	St.Petersburg	
	Ritz Carlton Moscow 5*	334		
	Marriott Grand Hotel 5*	392		
	Marriott Royal Aurora Hotel 5*	230		
	Marriott Tverskaya Hotel 4*	162		
Hyatt International	Ararat Park Hyatt Moscow 5*	219	Ekaterinburg	
Inter Continental Hotels Group	Holiday Inn Vinogradovo 4*	154	Samara	
	Holiday Inn Sushevski 4*	312		
	Holiday Inn Sokolniki 4*	523		
	Holiday Inn Lesnaya 4*	301		
	Crown Plaza	577		
Starwood Hotel & Resort	Le Meridian National 5*	221	St.Petersburg	Rostov on Don
	Le Meridien Moscow Country Club 5*	131		
	Sheraton Palace Hotel 5*	204		
Best Western International	Art-Hotel 4*	85	St.Petersburg	
Kempinski Hotels & Resorts	Balchug Kempinski 5*	232	St.Petersburg	
Accor Group	Novotel Sheremetievo 4*	488	St.Petersburg	
	Novotel Moscow City-Center 4*	257		
Small Luxury Hotels of the World	Savoy 5*	84		
Rezidor SAS Hospitality	Radisson SAS Slavjanskaya 4*	410	Sochi Rostov on Don St.Petersburg	Kaliningrad
Hilton Hotels Corporation	Hilton Moscow Leningradskaya 4*	279		Perm, Novosibirsk
Orco Group	MaMaison Pokrovka 5*	84		

Source: Department of External Relations, Moscow City Government and Industry Data

Figure 4 shows sales of restaurants at the Moscow hotels, including food and beverages.

Figure 4. Russia: Sales of restaurants at the Moscow hotels, including food and beverages



Source: The Mosvneshinform marketing company

*Average exchange rates by years: 2002 - \$1 = RUR31.3; 2003 - \$1 = RUR30.7; 2004 - \$1 = RUR 28.8; 2005 - \$1 = RUR 28.3; 2006 - \$1 = RUR 27.2

Luxury Hotels

The luxury hotel market, concentrated primarily in Moscow and St. Petersburg, is saturated. These hotels often feature cafes, bars, and restaurants with internationally recognized chefs. Unfortunately, hotel restaurants are rarely profitable. Since tourists only visit seasonally, hotel restaurants cannot rely exclusively on hotel guests for customers. The local population, however, does not regard hotel restaurants as “real” restaurants, even if they boast famous chefs. Hotel restaurants outside of Moscow and St. Petersburg (such as the new Radisson in Rostov-on-Don and the Park Inn Hotel in Yekaterinburg) may perform better due to a lack of other dining options. Despite the relatively flat growth in this sub-category, these hotels still 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, wine, and spirits are some of the better prospects for this segment.

Mid-Range Hotels

Mid-priced hotels do not usually have restaurant facilities. Some offer breakfast or other limited offerings. Most of these hotels are small enough that they purchase their food products from the local Cash & Carry or the retail market rather than from distributors. Some hotels contract with a local restaurant to provide food. Price is a very important consideration, and a large percentage of the products are domestically produced.

Budget and Economy Hotels

This includes hostels, apartments, and dorms. This segment does not offer many opportunities for foodservice. Few provide dining options, and customers in this segment usually rely on fast-food, cafes, and self-catering.

Institutions

Institutions are challenging customers for American producers. Before the 1990's, catering was a miniscule segment of the Russian hospitality market. Over the past four years, however, catering enjoyed a staggering annual growth rate of 30 to 70 percent, depending on the region. Catering is a quickly evolving industry, with Moscow claiming 62 percent of the market and St. Petersburg at 22 percent. There are an estimated 500 catering companies operating in Russia, including 30 major ones. Each year, 15 new companies enter and 20 companies exit this intensely competitive industry. Table 11 shows the market share of Russia's leading caterers.

Table 11. Russia: Catering Leaders, 2006

Company	Market share \$ million	Market share %	Number of customers in millions
Sodexho	44.5	26.2	5.4
Mega Foods	22.3	13.1	2.7
Parad Catering	14.8	8.7	1.8
Brizol	11.1	6.6	1.3
Master Food	8.9	5.2	1.0
Other	68.3	40.2	8.3
Total	169.9	100	20.7

Source: The Amiko consultancy

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 \$64 million in 2006. 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 grow, however, the office cafeteria is transforming. Corporate catering firms completely 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 \$5 to \$7. 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. Consequently, well-known restaurateur Arkadiy Novikov entered the catering business at the beginning of 2006. Other restaurateurs and five-star hotels are also rushing to enter this lucrative market, including Rosinter, 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 \$45 per person, but prices can be significantly higher in the premium class.

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 seasonings, nuts, meat, wine, and seafood.

While there is not yet a national school lunch program in Russia, there is interest in creating one. Packaging food for institutions may have some potential in Russia, but the cost and logistics of importing U.S. products may deter potential customers. Nevertheless, potential demand exists for rice, peas, beans, and lentils. Soup bases, spices, and institutional food packs could also appeal to some companies.

Universities, hospitals, and the army could be other potential customers for catering companies, but tenders are often not competitively bid for catering contracts with government institutions.

Recently, Russian Railways created a joint company with RP-Com, one of the top 10 foodservice operators in Moscow. They intend to build five commercial kitchens to cater to passengers on long-distance trains. The company is building its first catering facility near St. Petersburg and will serve hot meals to passengers on high-speed trains from St. Petersburg to Moscow. Other catering facilities will be built in Yekaterinburg, Novosibirsk, Sochi, and Rostov-on-Don. St. Petersburg's commercial kitchen will supply about 20,000 meal trays per day. Russian trains carried 1.3 billion passengers in 2007, including 137.7 million passengers on long-distance trains.

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 is currently building a kitchen facility in the Pulkovo airport. The volume of passenger traffic through Moscow's two main airports, Domodedovo and

Sheremetyevo, exceeded 30 million passengers in 2007 and is increasing annually by 15 to 20 percent. 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. Considering the increasing demand for high-quality airline food, airline foodservice could become an attractive niche market for U.S. food and beverage exporters.

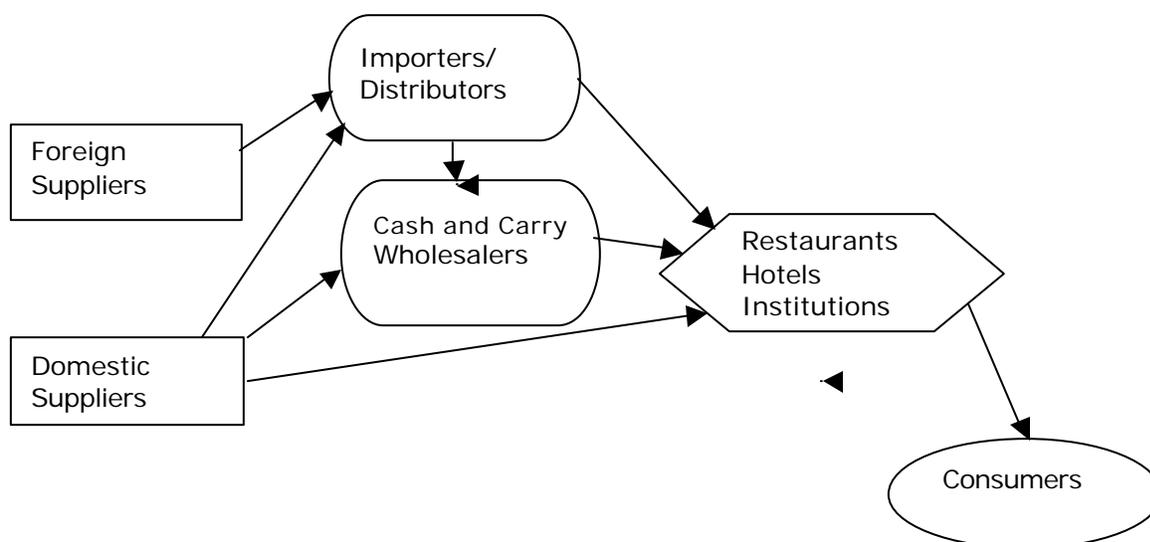
Another great opportunity for American producers and Russian foodservice operators will be the Sochi Olympic Games in 2014. The Russian government plans to renovate the Sochi airport, increasing capacity to serve 1,300 to 2,500 passengers per hour. In the buildup to 2014, Russia will construct restaurants, stadiums, and 57,000 hotel rooms to serve sports teams and guests. These will all provide a valuable potential market for American producers.

SECTION II: ROAD MAP FOR MARKET ENTRY

Distribution Channels for HRI Products in the Russian Market

Figure 5 shows the distribution channels for HRI products in the Russian market.

Figure 5. Russia: 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.

Advantages and Challenges for U.S. Products in Russia

Advantages	Challenges
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 handles volumes way beyond capacity, and there are complex customs regulations.
The relatively weak dollar makes U.S. exports more price competitive with Euro-zone products.	There is relatively low product awareness outside of U.S. poultry meat. Products need a lot of educational support and promotion.
Rising consumer incomes and changes in the consumption culture are creating new opportunities for high-quality products.	Increased health awareness influences consumption. There is a perception that American products contain unnatural hormones and chemicals.
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.
Growing inflation and rising food prices in Russia create export opportunities for U.S. commodities.	The Ministry of Agriculture is pushing to limit the number of importers for certain agricultural products in order to develop the Russian agricultural sector.
Russian trade and investment policy is converging with international standards.	There is continuing debate over World Trade Organization (WTO) accession and adherence to non-tariff barriers such as unscientific sanitary and phytosanitary restrictions that keep trade below potential.
In 2008, Russia will become the largest consumer market in Europe, according to the research "Russia: the largest consumer market in Europe" prepared by the analysts of the investment company Troika Dialogue.	There is excessive government bureaucracy, corruption, contradictory and overlapping regulations, economic vulnerability, and dependence on oil and mineral extraction for most wealth.

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. Several meat, seafood, wine, and spirits companies, however, are selling 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 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.

- **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 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.

While negative stereotypes about US products do exist, most interviewed HRI personnel said they were more interested in the quality and price of the food than in the origin. Negative stereotypes are more pervasive at the retail level, and restaurant consumers are not usually interested in the origin of their entrée.

- **Attend Promotional Events:** One of the main challenges for exporters entering the Russian market is product promotion. 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. If exporters are targeting specific regions within Russia, the Moscow ATO recommends participating in regional exhibitions.

Participation in trade shows, technical demonstrations, and trade missions to the U.S. are all marketing strategies that work well in the Russian market. The ATO recommends two interesting culinary-show opportunities in this area: PIR (Catering and Entertainment) Russia held each October, and the Vladivostok Culinary Festival, held each September. Participation in industry associations (USA Poultry and Egg Export Council, California Almond Board, etc.) that have a presence in Russia is also 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 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. As noted above, imports make up the vast majority of HRI products (more than 80 percent), with domestic suppliers filling the gaps.

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 2000. The company currently has 40 stores in Russia, including ten in Moscow and three in St. Petersburg. Foodservice operators across Russia have bought food, beverages, and other restaurant equipment from Metro Cash & Carry outlets.

Table 12 shows Russia's major suppliers of food products for restaurants.

Table 12. Russia: Major Suppliers of Food Products for Restaurants

Company	Principal Products	Country of origin	Customers	Locations
Emborg	Marbled Beef	USA, Australia	Hotels Restaurants Supermarkets	Moscow St. Petersburg 8 Russian regions
	Veal	USA, New Zealand		
	Beef	Russia, Brazil		
	Pork	USA, Denmark, Russia, Brazil		
	Fish and Seafood	Denmark, Norway, Spain, Asia		
	Poultry	France, Russia, USA, Brazil		
	Groceries	Poland, Germany, Russia, Netherlands		

East-West	Marbled Beef	USA, Australia	Hotels Restaurants	Moscow St. Petersburg Yekaterinburg
	Veal	USA, Australia		
	Beef	Russia, Brazil		
	Pork	USA, Russia, Brazil, Denmark		
	Lamb	New Zealand		
	Fish and Seafood	Norway, Spain, Thailand		
	Poultry	France, Russia, USA, Brazil		
	Groceries	Poland, Germany, Russia, Netherlands		
Global Foods	Marbled Beef	USA, Australia	Hotels Restaurants	Moscow St. Petersburg 8 Russian regions
	Veal	New Zealand, Australia		
	Beef	Russia, Brazil		
	Pork	Russia, Brazil, Europe		
	Lamb	New Zealand, Australia		
	Poultry	Russia, USA		
	Fish and Seafood	Norway, Spain, Russia		
	Groceries	USA, Europe, Russia		
Australia Trade House	Marbled Beef	Australia	Hotels Restaurants Supermarkets	Moscow
	Veal	Australia		
	Beef	Australia		
	Lamb	New Zealand, Australia		
	Fish and Seafood	Thailand, Vietnam, Russia		
	Butter	Australia		
Marr Russia	Marbled Beef	USA, Australia	Hotels Restaurants Supermarkets	Moscow St. Petersburg
	Beef	Brazil		
	Veal	Australia		
	Lamb	New Zealand		
	Pork	Hungary, USA, Russia		
	Poultry	Brazi, Russia		
	Fish and Seafood	Spain, Indonesia, Denmark		
	Groceries	Italy, Russia		
Snow World	Marbled Beef	USA	Hotels Restaurants	Moscow
	Veal	USA, Australia		
	Beef	New Zealand, Australia		
	Pork	Russia, Brazil		
	Lamb	New Zealand, Australia		
	Poultry	Hungary, France, Brazil		
	Fish and Seafood	Norway, Denmark, Russia, Asia		
	Groceries	Europe, Russia		

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. 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. High volumes enable large foodservice importers to gain better prices from global exporters.

The RFE and Siberia are highly dependant on imported foodservice products. 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. The majority of foodservice products are still shipped through Moscow, but meat, fish, seafood, cheesecake, and frozen bakery products are directly shipped from the U.S. to Vladivostok.

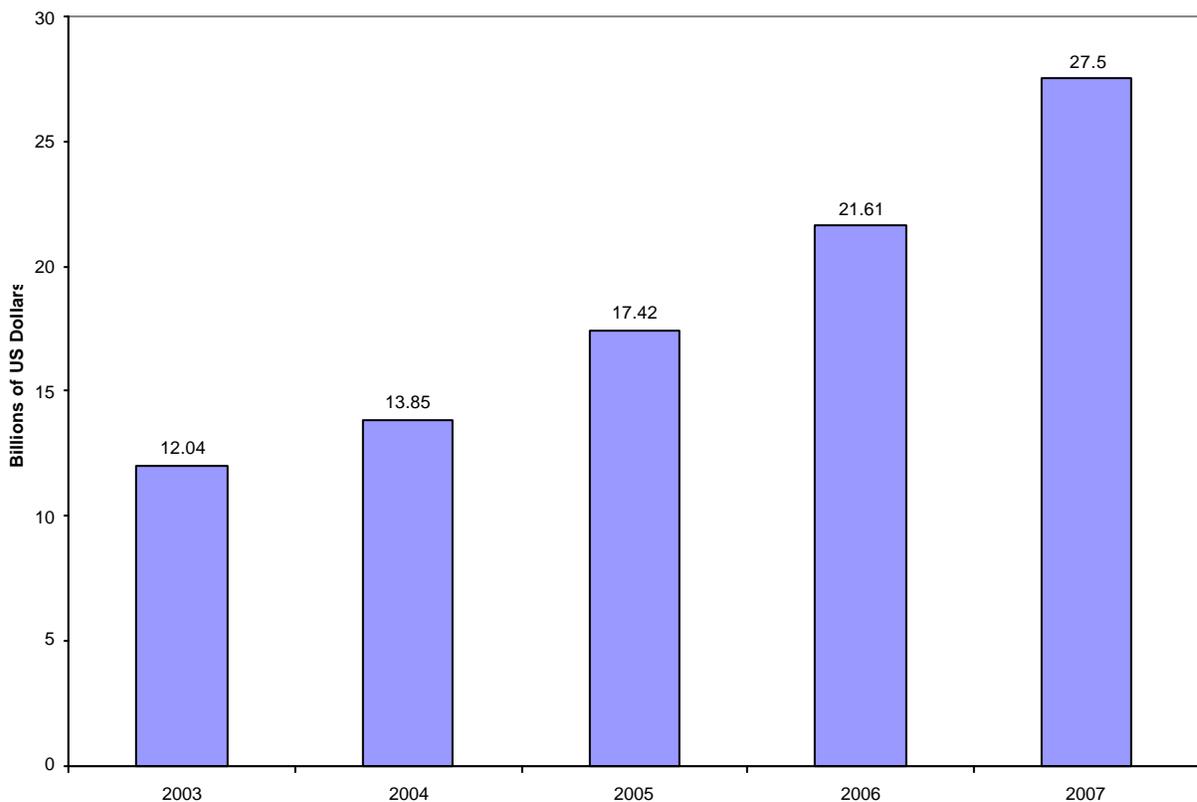
There is a new trend in foodservice logistics. Suppliers in Novosibirsk and other Eastern Siberia areas have started to order new products from Vladivostok importers. If Siberian suppliers continue to use Vladivostok importers, the product variety and import flow to the RFE could expand significantly.

Section III. COMPETITION

Russia imported approximately \$27.5 billion of agricultural products in 2007, an almost 400 percent increase from \$7.38 billion in 2000. Based on official data, the U.S. share exceeded \$1.3 billion. This is an underestimation, however, that does not account for transshipments via Europe. Poultry meat accounted for roughly three-quarters of a billion dollars, or more than half of the total, followed by pork, fish, nuts, edible offal, and fresh and dried fruit.

Figure 6 and Table 13 show the increase of Russian agricultural imports over time.

Figure 6. Russia: Agricultural Imports



Source: Federal Customs Service

Table 13. Russia: Imports of Selected Foods, 2005-2007

Product	2005		2006		2007	
	Value, \$ billion	Volume, MT	Value, \$ billion	Volume, MT	Value, \$ billion	Volume, MT
Fresh Beef	40.1	23.7	65.2	22.5	70.8	21.1
Frozen Beef	913.7	672.9	1529.4	647.2	1698.7	712.8
Pork	818.8	562.8	1394.9	625.6	1636.6	671.7
Poultry	847.5	1318.1	921.5	1274.2	1051.7	1287.3
Lamb	9.5	6.8	27.6	14.9	24.8	11.4
Fish and Seafood	950.6	868.8	1204.8	775.3	1731.1	997.9
Cheese	661.2	259.7	593.8	218.4	842.9	234.2
Dairy Products	22.9	15.9	19.6	13.3	35.2	24.5
Vegetables	722.4	1967.7	930.8	2143.1	1380.6	2304.1
Fruits & Nuts	2125.1	3998.1	2979.2	4659.5	3723.1	5087.1
Tea	312.4	179.4	354.5	172.9	431.2	181.3
Coffee	70.8	39.6	120.2	55.4	170.9	64.6
Cereals	249.3	1457.7	373.9	2310.1	298	1066.6
Sugar	930.7	3154.2	1280.1	2875.1	1394.2	3734.5

Source: Federal Customs Service

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 are Brazil, Germany, the United States, Ukraine, Argentina, the Netherlands, Poland, and China. No single country dominates the market.

The majority of products come from Europe. Europe's historical presence in Russia and aggressive promotional campaigns have allowed European brands to dominate even the RFE market. Poland and other Eastern European states are significant exporters of bread and bakery products. Since European companies can ship their products over land, they do not face the same port problems that U.S. imports confront. Consequently, they can provide perishables in a much faster manner. Major meat competitors include Brazil (poultry) and Australia (beef). Scandinavia, Asian countries, and occasionally South American countries are major seafood competitors.

Ukraine, Germany, and the Czech Republic are major beer suppliers. Italy, France, Spain, and the New World suppliers of Chile, Australia, and New Zealand are major wine suppliers. Californian wines appeared in Russia a few years ago, and sales are expanding rapidly. France, the United Kingdom and the U.S. supply popular spirits such as Bourbon, Tennessee and Scotch whiskey, cognac, and brandy.

Table 14 summarizes the major exporting countries of various products to Russia.

Table 14. Russia: Import Competition for Selected Products

Product	Country of Origin
Beef	Brazil, Argentina
Veal	Lithuania, Germany, Australia
Pork	Brazil, Denmark, USA
Poultry	USA, Brazil
Lamb	Australia, New Zealand
Fish and Seafood	Norway, Denmark, Asia
Dairy Products	Germany, Finland, Poland
Cheese	Germany, Ukraine
Vegetables	Netherlands, China, Turkey
Fruits & Nuts	Ecuador, Turkey, Argentina
Bread and Bakery	Europe
Ice-cream	Germany
Confectionary	Europe
Wine	France, Spain, Italy
Beer	Ukraine, Germany, Czech Republic
Spirits	France, United Kingdom, Ukraine, USA

Source: Federal Customs Service

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. Domestic potatoes are occasionally used, but this is often a last resort, since the size and quality are too inconsistent for restaurant use.

Section IV. BEST PRODUCT PROSPECTS

Local companies' interest in new product categories is growing. Many European specialty products are becoming more and more expensive. American products are consequently more price competitive and attractive to Russian importers. Importers are trying to find U.S. products analogous to European products. Table 15 shows Russian imports of selected U.S. food products.

Table 15. Russia: Russian Imports of Selected Food from the U.S., Billions of US Dollars

Product	2005	2006	2007	January – March 2008
Fresh Beef	0	0	0	0.153
Frozen Beef	0	0	0	0.351
Pork	43.511	148.116	180.388	78.987
Poultry	487.645	545.511	634.887	136.480
Fish and Seafood	43.477	44.108	51.672	12.164
Cheese	0.029	0.017	0.153	1.712
Fruits & Nuts	18.529	39.223	88.348	29.019
Tea	0.007	0.074	0.244	0.302
Coffee	0.106	0.167	0.157	0.082
Cereals	5.973	4.781	3.027	2.819
Sugar	4.536	5.239	8.782	2.510

Source: Federal Customs Service

This is an excellent time for American companies to export new products to Russia. Moreover, 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 poultry, pork and high-quality beef, cheese, and tree nuts are in demand. Exports of dairy to Russia are increasing, and, with the renegotiation of the veterinary certificate, it is expected that new export opportunities will be created.

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. Frozen breads may have potential, but they face competition from European suppliers.

There is some interest in organic foods, especially as Russia has no certification process for organics. Very few establishments in the HRI sector use or promote organics, but the market may be moving in this direction. The Novikov Group in particular has started marketing its own line of organic dishes in its restaurants.

Potatoes may also be appealing, but the current ban on U.S. potatoes prohibits trade. Potato products such as semi-prepared fries are allowed, but whole, raw potatoes are not. If this ban is lifted, this product has significant potential.

Wines and spirits also have high potential, but there is a lack of awareness about American wines. Alcoholic beverages also must comply with special rules regarding alcohol (see GAIN

reports RS7301 and RS7310). Figure 7 and Table 16 show the increase of wine and spirits imports from the U.S. over time.

Figure 7. Russia: Imports of Beverages from the U.S., in \$ billion

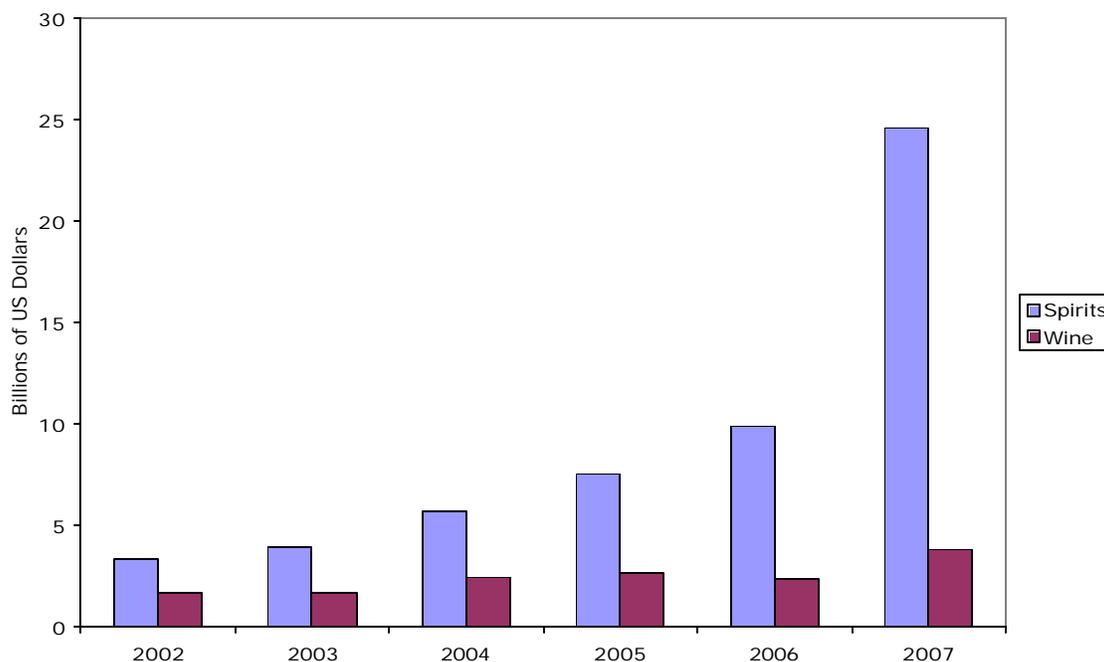


Table 16. Russia: Imports of Beverages from the U.S., in \$ billion

Product	2002	2003	2004	2005	2006	2007
Spirits	3.306	3.906	5.648	7.464	9.859	24.574
Wine	1.631	1.649	2.395	2.620	2.342	3.746
Beer	0.122	0.024	0.027	0.006	0.023	0.028

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

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 Daniil Schultz, Marketing Specialist
 Alla Putiy, Marketing Specialist
 Natalia Merinova, Administrative Assistant
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E-mail: atomoscow@fas.usda.gov

For mail coming from the U.S. (American officers only):

American Embassy Moscow
Agricultural Trade Office
5430 Moscow Place
Dulles, VA 20189-5430

For international mail, especially from Europe:

Agricultural Trade Office
U.S. Embassy - Box M
Itainen Puistotie 14
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Covering Northwest Russia (St. Petersburg):

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Covering Russian Far East (Vladivostok):

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32, Pushkinskaya Ulitsa
U.S. Consulate General
69001 Vladivostok, Russia
Tel/fax: 7 (4232) 300-089
atovladivostok@fas.usda.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:

Scott Reynolds, Agricultural Minister-Counselor (ETA August 10, 2008)
Mary Ellen Smith, Senior Agricultural Attaché (ETA August 11, 2008)
Erik Hansen, Agricultural Attaché
Office of Agricultural Affairs
American Embassy
(addresses as above for ATO Moscow)
Tel: 7 (495) 728-5222; Fax: 7 (495) 728-5133 or 728 5102
E-mail: agmoscow@usda.gov

To learn more about USDA/FAS and ATO services please visit <http://eng.usda.ru>.

Other Useful Contacts

The Agricultural Trade Office works with a large number of U.S. industry organizations, some of which have local offices to assist U.S. exporters of these food and agricultural products. You may also find these contacts listed at <http://eng.usda.ru>.

U.S.A. Poultry and Egg Export Council (USAPEEC)
E-mail: usapeec@usapeec.ru

U.S. Meat Export Federation (USMEF)
E-mail: Moscow@usmef.org

U.S. Wheat Associates
E-mail: uswmow@dol.ru

U.S. Grains Council (USGC)
E-mail: fgcmow@online.ru

Pear Bureau Northwest
E-mail: katerina@newmark.ru

Washington Apple Commission
Moscow office:
E-mail: office@bestapples.ru
Vladivostok office:
E-mail: katerina@newmark.ru

Almond Board of California
E-mail: Office@almondsarein.ru

Wine Institute of California
E-mail: olgatuz@mail.ru

Pet Food Institute
E-mail: agerman@globalworks.ru

National Renderers Association
E-mail: lischenko@ane.ru

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

American Chamber of Commerce in Russia (AmCham)

Ul. Dolgorukovskaya, Building 7, 14th floor

127006 Moscow, Russia

Tel: 7 (495) 961-2141; Fax: 7 (495) 961-2142

<http://amcham.ru/>

Email: amchamru@amcham.ru

American Chamber of Commerce in St. Petersburg

25 Nevsky Prospect, 3rd Floor

191186 St. Petersburg, Russia

Tel: 7 (812) 326-2590; Fax: 7 (812) 326-2591 or 326-2561

<http://amcham.ru/spb/>

Email: st.pete@amcham.ru

For questions regarding agricultural machinery, food processing and packaging equipment or materials, refrigeration equipment, and other industrial products, please contact:

U.S. and Foreign Commercial Service

Bolshaya Molchanovka, 23/38, Bldg. 2

121069 Moscow, Russia

Tel: +7 (495) 737-5030; Fax: +7 (495) 737-5033

E-mail: moscow.office.box@mail.doc.gov

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://www.fas.usda.gov/scriptsw/AttacheRep/default.asp>

RS8055 FAIRS Country Annual Report

Not yet posted

RS8045 Organic Products / New SanPIN for Organic Products

<http://www.fas.usda.gov/gainfiles/200806/146294938.pdf>

RS8030 Fish Trade Update

<http://www.fas.usda.gov/gainfiles/200804/146294325.pdf>

RS8029 Russia Lifts Ban on U.S. Rice Imports

<http://www.fas.usda.gov/gainfiles/200804/146294319.pdf>

RS8020 Exporter Guide / Agriculture and Agribusiness Consultants

<http://www.fas.usda.gov/gainfiles/200803/146294084.pdf>

RS8005 2008 Meat and Poultry Duties Change

<http://www.fas.usda.gov/gainfiles/200801/146293553.pdf>

RS7336 Retail Food Service Annual

<http://www.fas.usda.gov/GainFiles/200712/146293276.pdf>

RS7335 Fresh Deciduous Fruit

<http://www.fas.usda.gov/gainfiles/200712/146293158.pdf>

RS7334 Exporter Guide / Annual

<http://www.fas.usda.gov/gainfiles/200711/146293117.pdf>

RS7081 Products Subject to Border Veterinary Inspection

<http://www.fas.usda.gov/gainfiles/200711/146292933.pdf>

RS7073 Poultry and Products / Annual

<http://www.fas.usda.gov/gainfiles/200710/146292768.pdf>

RS7071 Dairy and Products / Certain Dairy Import Tariffs Reduced

<http://www.fas.usda.gov/gainfiles/200710/146292751.pdf>

RS7069 Export Certificates / Annual

<http://www.fas.usda.gov/gainfiles/200710/146292717.pdf>

RS7061 Food and Agricultural Import Regulations and Standards / Annual

<http://www.fas.usda.gov/gainfiles/200709/146292471.pdf>

RS7051 Government Program for Agriculture and for Market Regulation 2008-2012

<http://www.fas.usda.gov/gainfiles/200707/146291764.pdf>

RS7020 Progress of the National Priority Project in Agriculture

<http://www.fas.usda.gov/gainfiles/200702/146280251.pdf>

RS7011 List of Products that Require Quarantine and Phytosanitary Certificates

<http://www.fas.usda.gov/gainfiles/200707/146291722.pdf>

RS7008 Russia Lowers Out-of-Quota Import Duties on Beef

<http://www.fas.usda.gov/gainfiles/200701/146280054.pdf>

RS6321 Growing Russian consumerism propels retail increases

<http://www.fas.usda.gov/gainfiles/200612/146269877.pdf>

Wine and Spirits

RS7323 FAIRS Product Specific / Wine

<http://www.fas.usda.gov/gainfiles/200707/146291722.pdf>

RS7310 Wine and spirits: New bank guarantee requirement limits import growth

<http://www.fas.usda.gov/gainfiles/200704/146280895.pdf>

RS7304 Russian wine and spirits regulations updated

<http://www.fas.usda.gov/gainfiles/200703/146280405.pdf>

RS7301 New health label required for wine and spirits

<http://www.fas.usda.gov/gainfiles/200702/146280194.pdf>