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Food Service - Hotel Restaurant Institutional

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Report Highlights:

The restaurant sector in Russia has faced a number of serious challenges in 2014. A food import ban from numerous countries announced in August 2014, implementation of a smoking ban in restaurants and bars, a weakening ruble, currency fluctuations, dropping consumer purchasing power has many hotels, restaurants, and institutions (HRI) struggling to stay open. Market analysts forecast 30 percent of all restaurants in Russia to shut down by spring 2015. Investment in hotels in Russia has been very attractive in recent years driven by limited supply of quality lodging facilities, low overall competition, gradually improving business climate, and growing domestic and foreign travel volumes.

Executive Summary:

The restaurant sector in Russia has faced a number of serious challenges in 2014. A food import ban from numerous countries announced in August 2014, implementation of a smoking ban in restaurants and bars, a weakening ruble, currency fluctuations, dropping consumer purchasing power has many hotels, restaurants, and institutions (HRI) struggling to stay open. Market analysts forecast 30 percent of all restaurants in Russia to shut down by spring 2015.

Investment in hotels in Russia has been very attractive in recent years driven by limited supply of quality lodging facilities, low overall competition, gradually improving business climate, and growing domestic and foreign travel volumes. One of the recent trends is the growth of hotels in regional cities of Russia due mainly attributable to the large-scale international events taking place throughout in Russia. Before the recent devaluation of the Russian ruble and news of contracting economic indicators were announced, it was estimated that by 2017, the number of hotels under international management would increase by 157 new operators (32,000 rooms).

SECTION I: MARKET SUMMARY

According to the Russian Federal Statistics Service (Rosstat) data, Russia's GDP growth in 2013 was 1.3 percent. Unemployment was at a record low 5.5 percent % in 2013 and has remained stable since 2012. Inflation in 2013 was 6.5%. In addition, individuals' real incomes in 2013, increased by 12.5% compared to 2012. Positive GDP due to high oil prices which are the main drivers of the Russian economy, individuals' real incomes increase, and a record-low unemployment rate add up to growing consumer purchasing power in Russia.

Russia has faced a number of serious challenges in 2014. A food import ban from numerous countries announced in August 2014, a weakening ruble, dependent of oil prices, which declined to their lowest level since 2010, currency fluctuations, high inflation have dropped consumer purchasing power.

Table 1: Russia: Social and Economic key figures

	2009	2010	2011	2012	2013	2014* forecast
Population, million.	142.8	149.2	143	143.3	143.7	146.1
Unemployment, % of labor force	8.3	7.3	6.5	5.5	5.5	
Average monthly salary per person, RUR	18638	20952	23369	26629	29960	in October 32250
Real GDP growth, % change y-o-y	-7.9	4.5	4.3	3.4	1.3	0.6
Inflation, %	8.8	8.8	6.1	6.6	6.5	9.4 in mid December
Exchange rate (per \$1)	31.76	30.36	29.35	31.07	31.9	38

Source: Federal State Statistics Service (Rosstat)

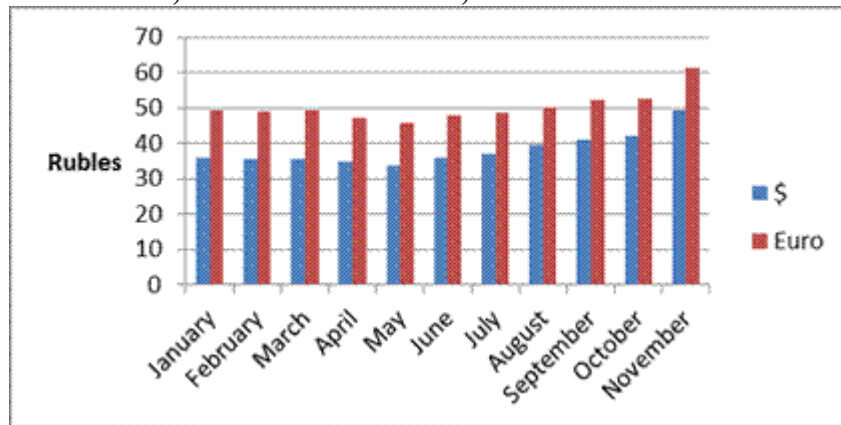
*Forecast for 2014

Russia is the ninth most populous country in the world with more than 143 million people. European Russia, geographically west of the Urals, hosts over 75 percent of the total population, although it accounts for only 25 percent of the country's territory. According to Rosstat, 74 percent of all Russians lived in urban areas in 2012 and over 10% of the total population lived in Moscow (11.98 million

people) and St. Petersburg (5.03 million people). Beyond the two largest Russian cities there are thirteen cities (Novosibirsk, Nizhniy Novgorod, Yekaterinburg, Samara, Omsk, Kazan, Ufa, Chelyabinsk, Rostov-on-Don, Volgograd, Perm, Krasnoyarsk, Voronezh) with a population of more than one million people.

Russia is very dependent of oil prices, which declined to their lowest level since 2010 following OPEC's November 27, 2014 decision not to reduce its daily output quota, putting substantial depreciation pressure on the Russian ruble. The ruble fell below the RUB 50/\$1 level during trading in Moscow November 28, and the Central Bank of Russia announced the official rate for November 29 at RUB49.322. Since the beginning of 2014, the ruble has depreciated by a little over 51 percent against the dollar. The ruble fell to 65.45 rubles/USD and 78.87 rubles/euro on December 15, prompting the Central Bank of Russia to raise its key interest rate by a massive 6.5 percentage points to 17 percent.

Figure 1. Russia: Central Bank's Exchange Rate of \$1 USD to Ruble and \$1 Euro to Ruble from December 1, 2013 to November 1, 2014



Source: Central Bank of Russian Federation

In August 2014, Russia banned imports of beef, pork, poultry, fish, cheese, dairy products, fruit and vegetables from Australia, Canada, Norway, the U.S. and the E.U. for one year as an answer to Western sanctions. Russian food imports fell 11.3 percent on the year in September to \$2.9 billion in the wake of the ban. Inflation has inevitably been pushed up by the reduced supply of goods— noting that an insufficient level of competition in Russia allows manufacturers and retailers to up their prices. Inflation is also impacted by the additional transport costs associated with buying products from further afield – notably from South America. In some cases these, extra costs may involve the re-routing of European products through Belarus. Year-on-year inflation hit 8 percent in September, driven up by the declining value of the Ruble and Russia's ban on many food products from the United States and European Union, according to data from Russian Federal Statistics Service (Rosstat). Rising food prices were the main driver, climbing 11.4 percent year-on-year in September, up from a 10.3 percent increase year-on-year in August. Food price rises have been key factor behind inflation, but it has also been driven by steady devaluation of the ruble. In August, real wages in Russia fell 1.2 percent - the first time real wages have fallen since 2009. Rising inflation, higher food prices, a weakening ruble, and falling consumer purchasing power is leading many Russians to lessen visits to restaurants and to switching from higher level restaurants to more affordable restaurants such as fast food type establishments.

HRI Sub-Sectors

Restaurants

Restaurant sales during the first 10 months of 2014 totaled 986.7 billion rubles but most of the sales took place in the first half of the year. According to market analysts, since July 2014, Russia's restaurant industry has seen a decline of around 15 percent for the first time since 2010. Food service turnover is expected to surpass 1.2 trillion rubles by the end of 2014. Fast food outlets and coffee houses are the most popular and fastest-growing sectors in Russia and are in better situation in comparison to fine dining and mid-range restaurant. Currently the largest cities in Russia, Moscow and St. Petersburg, account for 41 percent and 15 percent respectively in terms of chain outlets on the overall consumer foodservice market. Moscow and St. Petersburg remain the leaders in HRI concentration and growth as well as the industry trend-setters. These two cities control 14 percent of Russian foodservice market. High operational costs in Moscow and St. Petersburg, and the fact that the foodservice market in both cities is highly saturated, are forcing the main players to consider regional expansion in order to sustain their share. The foodservice market in the regions of Russia is still relatively underdeveloped and has strong potential for further growth.

Franchising and sub-franchising has become a very popular tool for multinational and local players in Russia. Franchising offers an easier way for investors to enter the Russian market with a lower level of investment, since the materials required for the setting up of outlets and apparatus are often included as part of the franchise agreement, cutting expenses and bringing about profits more quickly. Decline of different foodservice sectors differ. Fast food outlets and coffee houses are the most popular and fastest-growing sectors in Russia and are in better situation in comparison to fine dining and mid-range restaurant.

Table 2. Russia: Food Service Industry Sales in Russia

	2009	2010	2011	2012	2013
RUR, billion	711.2	781.4	903.3	1013.6	1131.3
Growth Year on Year, %		9.8	15.6	12.2	11
US Dollars, billion	22.42	25.63	30.77	32.62	35.46
Average exchange rate	31.72	30.48	29.35	31.07	31.9

Source: Federal State Statistics Bureau (Rosstat)

Major Restaurant Operators in Russia

According to Rosstat, the number of cafes, restaurants, and other food outlets in Russia currently stands at about 88,000 and almost 88 percent of outlets are independent (non-chain) cafes and restaurants. In 2013 the number of foodservice chain outlets increased by 8 percent, the total increase during 2007-2012 constituted 63 percent. According to FoodService magazine there are currently more than 370 restaurant chains operating in Russia, each of which manages between 3 - 900 outlets. Total number of chained restaurant currently is about 11000 outlets. McDonald's, Subway, Rosinter Restaurant Holding, Arkadiy Novikov Restaurants, Ginza project, Markon, Shokoladnitsa are the largest restaurant chains in different foodservice segments in Russia.

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

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

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

The fastest growing segments are fast food and coffee shops. Consumers still considered dining in full-service restaurants as a less essential activity due to the fact that these outlets usually have higher average prices compared with fast food establishments or cafés/bars, and they remained budget-conscious when dining in such outlets.

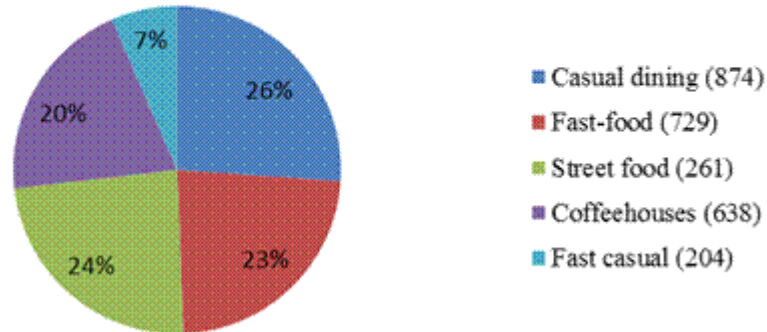
Table 3. Russia: Consumer Foodservice by Independent versus Chain Outlets, 2012

Outlets	Independent	Chained	Total	% of Total
Fast-food	16,722	5,320	22,042	25
Street stalls/kiosks	11,170	1,603	12,773	14.5
Cafés/bars	9,171	1,214	10,385	11.8
Full-service restaurants	5,859	1,325	7,184	8.1
Pizza consumer foodservice	3,026	878	3,904	4.4
Self-service cafeterias	31,094	80	31,174	35.4
100% home delivery/takeaway	534	168	702	0.8
Total	77,576	10,588	88,164	100

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

In many aspects, including the increase of outlet quantity, the market is driven by foodservice chains and Moscow is not an exception of this trend.

Moscow chained restaurants shares by segments with # of outlets



Source: RBC research, May 2013

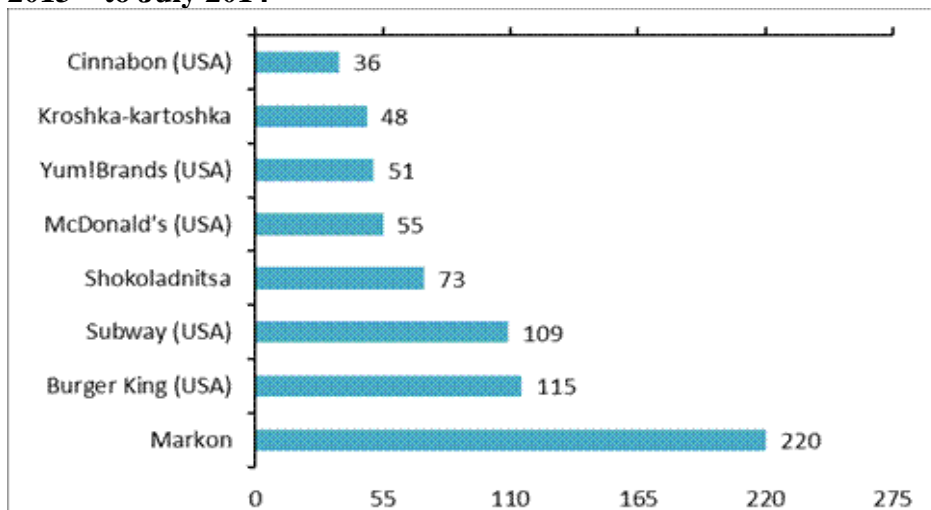
Table 4. Russia: Leading Foodservice Restaurant Companies, July 2014

Holding company	# outlets in Russia	% y-o-y change 2014	# outlets in Moscow	Brands	Type
Markon	905	32.1	405	Stardog!s, Bageteria	Street + QSR
Subway	691	18.7	191	Subway	QSR
Shokoladnitsa	434	20.2	278	Shokoladnitsa, Vabi Sabi	QSR + casual
McDonald's	433	14.6	184	McDonald's, McCafe	QSR
Kroshka-Kartoshka	368	15	262	Kroshka-Kartoshka	Street + QSR
Rosinter	323	1.3	199	Il Patio, Planet Sushi, other	Casual
BRPI	300	8.5	98	Baskin Robins	QSR
G.M.P. Planeta Gostepreimstva	294	-0.7	139	Sbarro, Vostochnyy bazar, Yolki-Palki	QSR + casual
Yum!Brands	281	22.2	113	KFC	QSR
Teremok	247	14.9	118	Teremok	Street + QSR
Burger King Rus	228	101.8	122	Burger King	QSR
Coffee House	191	-8.6	117	Coffee House, Asia, Vinegret	QSR + casual
Podorozhnik	157	6.1	0	Podorozhnik	Street + QSR
Cinnabon	144	33.3	16	Cinnabon	QSR + casual
Yevrasia	143	-5.4	0	Eurasia	Casual

Ginza Project	97	3.2	88	Yaposhka and different concept restaurants	Fine + casual
Novikov Group	88	-2.2	87	Different concept restaurants	Fine + casual

Source: FoodService magazine 2014

Figure 2. Russia: Growth of Leading Foodservice Restaurant Companies by # of Outlets from July 2013 – to July 2014



Source: FoodService magazine 2014

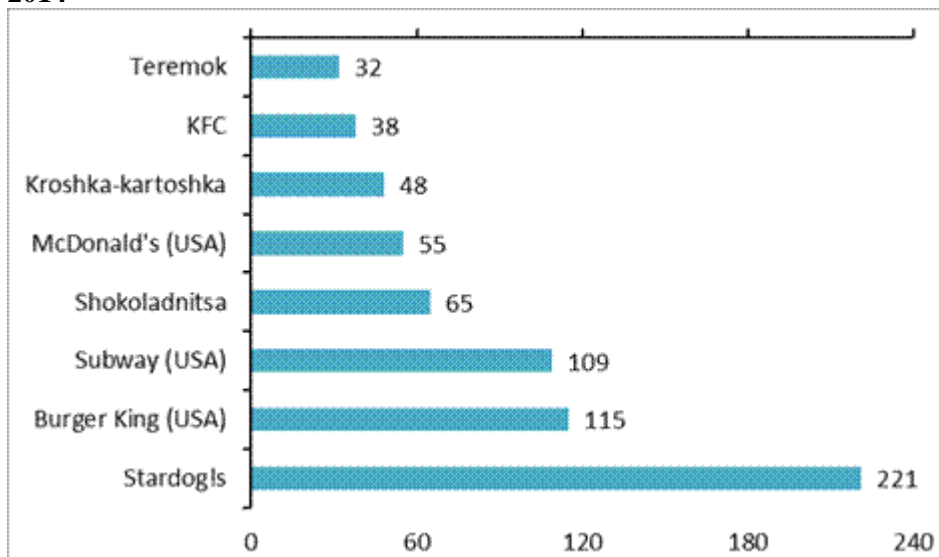
Table 5. Russia: Leading Foodservice Brands, July 2014

Brand	# outlets in Russia	% y-o-y change 2014	Holding company	Type	Country of origin	Year est. in Russia
Stardog!s	905	32.1	Markon	Street + QSR	Russia	1993
Subway	691	18.7	Subway	QSR	USA	1994
McDonald's	433	14.6	McDonald's	QSR	USA	1990
Shokoladnitsa	408	19.2	Shokoladnitsa	QSR + casual	Russia	2001
Kroshka-Kartoshka	368	15	Kroshka-Kartoshka	Street + QSR	Russia	1998
Baskin Robins	300	8.5	BRPI	QSR	USA	1992
KFC	268	16.5	Yum!Brands		USA	1993
Teremok	247	14.9	Teremok	Street + QSR	Russia	1998
Burger King Rus	228	101.8	Burger King	QSR	USA	2010
Coffee House	182	-8.6	Coffee House	QSR + casual	Russia	1999
Podorozhnik	157	6.1	Podorozhnik	Street + QSR	Russia	1995
Sbarro	147	2.1	G.M.P. Planeta Gostepreimstva	QSR + casual	USA	1997

Yevrasia	143	-5.4	Eurasia	Casual	Russia	2001
Il Patio	185	3.8	Rosinter	Casual	Russia	1993
Cinnabon	111	8.8	Cinnabon	QSR + casual	USA	2009
Planeta Sushi	111	-0.9	Rosinter	Casual	Russia	1999

Source: FoodService magazine 2014

Figure 3. Russia: Growth of Leading Foodservice Brands by # of Outlets from July 2013 – July 2014



Source: FoodService magazine 2014

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 at meal's end in Moscow and St. Petersburg. Fine-dining restaurants are associated with names such as Arkadiy Novikov, Andrey Delos, and Ginza Project, but most experts agree that the top-category restaurant sector is saturated. Restaurateurs are moving toward casual restaurants where tables turn over more quickly and profit margins are higher. Nevertheless, there is still an opportunity for U.S. products in the fine dining segment because consumers are loyal to high-quality imported products such as marbled beef, seafood, high-end wines, and spirits.

Ginza Project is one of the largest consumer foodservice businesses in Russia. The company operates various restaurants and entertainment venues with different formats and price segments, although there is a bias towards various fine dining options. The restaurant holding Ginza Project began developing a nationwide network of Yaposha cafés in 2003. Since 2008, Ginza Project has continued to invest heavily in its expansion. The group opened its themed restaurants in Moscow, St. Petersburg, Rostov-on-Don, and New York. As of December 2013, the company operates 97 outlets, including 88 restaurants in Moscow. Currently company has focused on development democratic restaurant Paul's bakery shops.

Arkadiy Novikov Restaurant Group (Novikov Group) includes nearly 90 restaurant-retail-entertainment projects of various formats and price ranges. The company has launched and managed restaurants since 1992 and has continued to place second in full-service restaurants. The Novikov Group is slightly less chain-oriented. It operates more than 50 different Moscow high-end concept restaurants, along with a five casual-dining restaurant chains such as, Sushi Vesla, Prime Star, and Kish-Mish. It also operates the premium grocery chain Globus Gourmet, the Russian branch of the French gourmet chain Hediard, the greenhouse complex OOO Agronom, and the Premium Class catering business. Novikov has also branched out internationally and has a restaurant in London named Novikov Restaurant and Bar. Since 2013 Company has developed Krispy Kreme doughnut café chain.

Casual-Dining Restaurants

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

North American-style steakhouses, Japanese cuisine, and European restaurants are very popular in Russia. More than 50 percent of the food it serves up is imported. Some hard to replace items like French and Italian cheeses, Norwegian salmon, Australian ribeye steak, Finnish butter and even cheap American drumsticks, and seafood are heading off the menu at restaurants after the ban on imports of all fish, meat and dairy produce. This is extremely difficult situations for the fine dining and even mid-range restaurant which serves sushi, seafood and have European menus.

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

The enormous popularity of Japanese cuisine made Asian full-service restaurant chains the most ubiquitous category of casual restaurants. Japanese restaurants, with sushi and fish menus, are heavily represented among fish and seafood-concept restaurants in Russia. Currently Japanese restaurants are in difficult situation due to Russian food ban. It's difficult to find substitutions of Norway salmon. After the August 2014 ban suppliers of salmon from Chile and the Faroe Islands to Russian have almost doubled their prices. A Russian importer reported that Faroe exporters have increased prices from \$6.25/kg to \$10/kg. Chilean sellers have also stopped credit lines for Russian buyers, asking for pre-

payments on orders. Restaurant experts predict reduction of Japanese restaurant in nearest future.

Very few casual chain restaurants have a centralized system of purchasing. Most decisions regarding products and purchasing are made at the restaurant/group level. On the one hand, there are many more opportunities for sales, since each restaurant is a separate account. On the other hand, individual sales are smaller and do not allow for the development of exclusive distribution rights and consistent volumes.

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. After the food sanctions Russian restaurateurs are trying to use as much local products as possible and are developing Russian, Georgian and Uzbek cuisine.

Rosinter Restaurants Holding (Rosinter) is a major player on the Russian restaurant market. The company gained its leadership role by its early deployment of chain restaurants in the casual-dining segment of the market where Rosinter held about 9 percent of the market in 2013, or 355 outlets in Russia, the CIS, Central Europe, and the Baltic states. Rosinter's consolidated net revenue decreased by 2.2 percent in 2013 and stood at 9.84 billion rubles because of restaurant portfolio optimization.

Rosinter's sale for January-June of 2014 was 4.7 billion rubles.

The company offers Italian, Japanese, American, and Russian cuisine under its proprietary brands (Il Patio, Planet Sushi, American Bar & Grill, and Mama Rasha) and its licensed brands (T.G.I. Friday's, Costa Coffee, and McDonald's). Il Patio and Planet Sushi are among the most recognized brands in Russia and around 19 million guests a year visit Rosinter's outlets.

Table 6. Russia: Rosinter Restaurant Brands, September 2014

Brand name	Type	First year of operation in Russia	# outlets Corporate	# outlets, Franchised
Planet Sushi	Casual (Asian)	1999	65	62
Il Patio	Casual (Italian)	2005	80	69
T.G.I. Friday's	Casual (American)	1997	23	-
American Bar & Grill	Casual (American)	1994	8	-
Costa Coffee	Coffee house	2008	30	-
Other			18	
Total			224	131

Source: Rosinter data

Table 7. Russia: Rosinter Consolidated Revenues in 2008-2013

	2008	2009	2010	2011	2012	2013
RUR, billion	8.36	8.34	9.17	10.34	10.57	9.84
Growth Year on Year, %		-0.3	9.9	12.8	2.2	-7.1
US Dollars, million	336.55	262.93	300.85	352.30	340.10	308.34
Average annual exchange rate	24.84	31.72	30.48	29.35	31.07	31.9

Source: Rosinter data

Rosinter has three main development 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 April 2012, Rosinter received rights under an agreement through April 2023 to operate McDonald's restaurants in Moscow's three international airports and St. Petersburg's Pulkovo airport. In December 2013, first McDonald's was opened in St. Petersburg's at the new terminal of Pulkovo Airport.

RP-Com (Restaurant Professional Company) is one of the top 20 foodservice operators in Moscow. RP-Com currently owns the following restaurants in Moscow: twelve Goodman steakhouses (also with branches in Novosibirsk, London, Zurich and Kiev), two Filimonova & Yankel fish-houses, seven Kolbasoff beer-restaurants. During its ten years of foodservice experience, the company has gained success in the niche of steak house restaurants. This type of restaurant is less developed in Russia, and currently only a few independent operators specialize in grill menus. The Goodman chain became the largest chain of North American full-service restaurants in Moscow as well as in the whole of Russia.

RP-Com belongs to the Food Service Capital Group of companies which also includes "Comfis" prepared food factory, "Legion" food provider, Saint Petersburg prepared rations factory and food service company providing passenger meals for Sapsan high-speed trains.

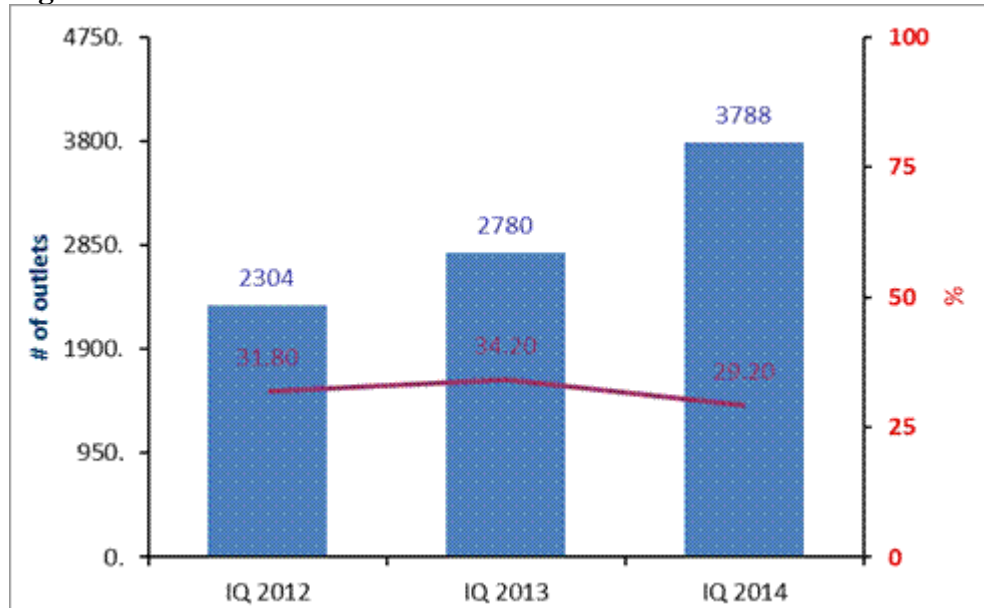
In September, a popular sushi chain Yevraziya, closed 10 outlets in its home city St. Petersburg, and sold off all 15 of its restaurants in Moscow. Russians love sushi, and Japanese restaurants have flourished over the past few years. But one of Yevraziya's owners says his chain is being squeezed from two sides: Russian sushi lovers have less money to spend, and the price of supplies has skyrocketed.

Fast Food

Fast food remained one of the main foodservice drivers in 2013 and continues to grow in 2014. Chained fast food is performing particularly well recording current value growth of 29 percent in 2013. This strong growth can mainly be attributed to the growing popularity of franchising in Russia. Without a doubt, franchising is becoming one of the main tools of fast food business development, especially in the chained segment. This reflects Russian customers' preference for well-known and stable foodservice standards provided by the chained segment – a fact which is confirmed by outlet growth as well, with the number of independent fast food outlets increasing only marginally in 2013, chained fast food outlets increasing by 15 percent. Approximately 100 fast food operators manage almost 3,800 chain restaurants in Russia. According to expert estimates fast food market in Russia will reach 400 billion rubles in 2014.

Today fast food is the most popular segment for young and middle-aged Russian consumers. Research has shown that more than 54 percent of fast food restaurants visitors are from 18 to 34 years old with average monthly income of 30,000 rubles. While the economic slowdown and currency devaluation are slowing down fast food expansion in Russia, research has shown that Russians are switching from higher end restaurants to mid-level and fast food type establishments which should help fast food chains weather the challenging times ahead.

Figure 4. Russia: Number of Fast Food Chained Restaurants in Russia in 2012-2014



Source: RBC research

According to Head of Russian Franchise Association, today foodservice market sees some shift of customers from expensive restaurant formats to casual places with affordable prices. Currently about 70 percent of the residents of major Russian cities several times a month have visiting fast-food outlets with average checks of 150-300 Rubles (\$5-\$10) on a regular basis. Pancakes, burgers, sandwiches, chicken, pizza, and baked potatoes are the most popular types of fast-food in Russia.

Table 8. Russia: Fast Food Formats in Russia

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

Source: Fast food market research

Fast-food restaurant chains tend to use a higher percentage of local ingredients (around 70-85 percent) as compared to other restaurants and charge much less. Several fast-food chains have created internal supply-chains based in Russia in recent years. For example McDonald's, which operates roughly 450 restaurants throughout the country, gets 85 percent of its menu items from domestic suppliers.

Transnational chains have demonstrated most impressive fast food development since 1990. Franchising is one of key expansion methods for foodservice chains in Russia. According to expert estimates share of foreign brands on Russian restaurant market is about 40 percent. American fast food formats dominate in Russia and have fastest growth; among them are Subway, McDonald's, Burger King, and Baskin Robbins.

Table 9. Russia: Growth of Fast Food Restaurant Chains in Russia, 10 leading chains

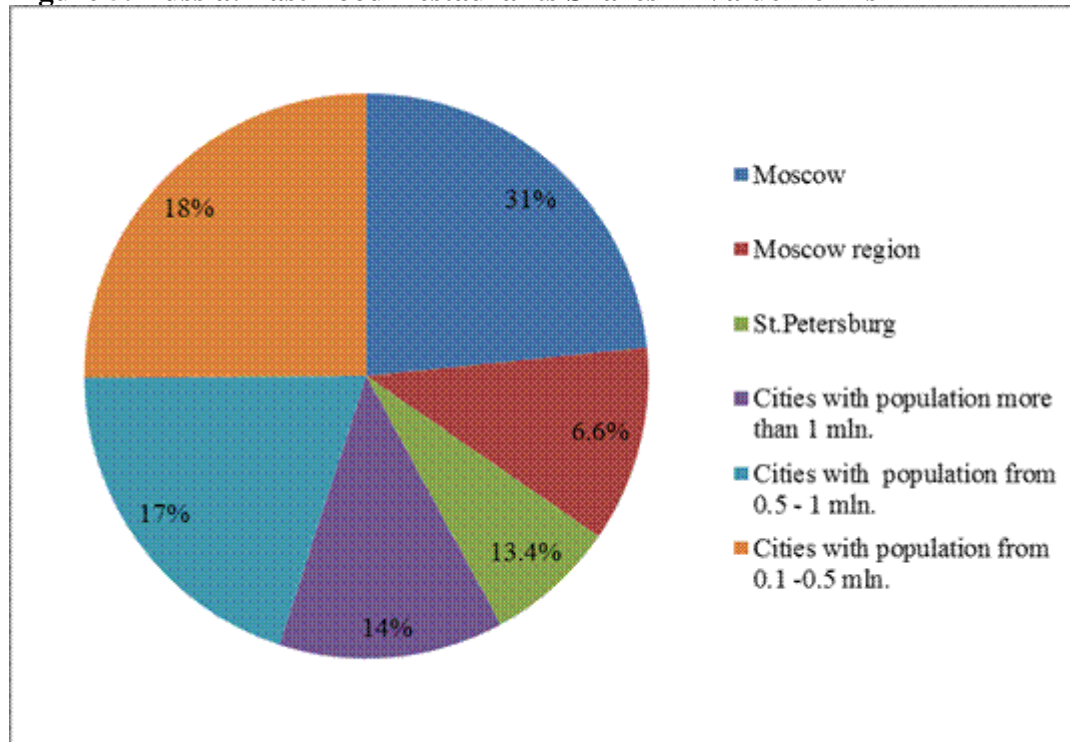
Chain name	Country of origin	Year est. in Russia	# outlets July,2013	# outlets September, 2014	% change for 14 months
Stardog!s*	Russia	1993	685	758	10.6
Subway	USA	1994	582	704	20.9
33 Penguins	Russia	2004		485	
McDonald's	USA (Canada)	1990	378	444(435)	15.1
Kroshka-Kartoshka	Russia	1998	320	373	16.6
Baskin Robbins	USA	1992	274	327	19.3
KFC	USA	1993	230	290	26.1
Teremok	Russia	1998	215	251	16.7
Burger King	USA	2010	113	235	108
Sbarro	USA	1998	144	160	11.1
Podorozhnik*	Russia	1995	148	153	3.3

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

*street-food kiosks

According to the RBC research, 31 percent (1,178 of 3,788) of fast-food restaurants are successfully operating in Russia's capital. St. Petersburg today accounts for slightly more than 13 percent (503 of 3,788) fast-food restaurants.

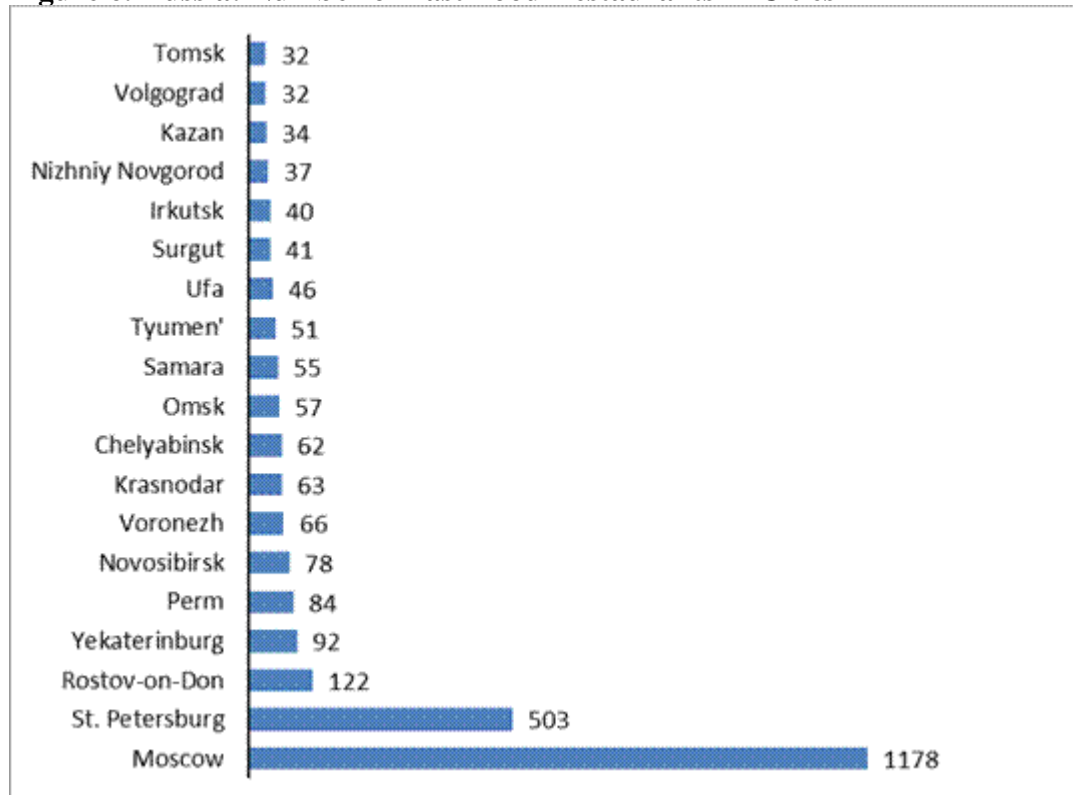
Figure 5. Russia: Fast Food Restaurants Shares in Value Terms



Source: RBC research, May 2014

Almost half (44.4 percent) of all fast food restaurants in Russia are concentrated in Moscow and St. Petersburg of which combined have only 12 percent of the total population. Thus, 55.6 percent of the remaining fast-food restaurants cater about 88 percent of the Russian population. In this context, the relatively high level of competition in Moscow and St. Petersburg is pushing many franchises to more actively open fast food restaurants in regions. Beyond the two largest Russian cities there are thirteen cities (Novosibirsk, Nizhniy Novgorod, Yekaterinburg, Samara, Omsk, Kazan, Ufa, Chelyabinsk, Rostov-on-Don, Volgograd, Perm, Krasnoyarsk, and Voronezh) with a population of more than one million people.

Figure 6. Russia: Number of Fast Food Restaurants in Cities



Source: RBC research, May 2014

International franchises doing business in Russia include Burger King, Subway, Baskin-Robbins, Dunkin' Donuts, and KFC with the franchise system are most prevalent in Moscow and St. Petersburg. The most dynamic chains -- including Subway, Burger King, KFC, Kroshka-Kartoshka, and Baskin-Robbins -- have opened numerous outlets in shopping malls and hypermarkets.

As of September 2014, leader of fast food restaurants **Subway** had 704 outlets in all Russian regions, including the Far Eastern Federal District. Subway is one of the most rapidly developing fast food chains in Russia. In 2011, Subway managed to outrun McDonald's in terms of outlets in Russia. Subway maintains an ambitious plan of expansion.

Former leader in terms of quantity of chain eating places **McDonald's** is the leader of Russian fast food market in value terms. McDonald's entered Russia in 1990 and opened its first restaurant in the center of Moscow. As of September, 2014 McDonald's had more than 435 restaurants in 85 Russian cities, including McCafes, operating throughout Russia and serving about 1 million customers daily. On McDonald's 20th anniversary in Russia in January 2010, company reported about serving 2 billion customers.

Until April 2012, McDonald's had been expanding in Russia through self-operated stores only.

McDonald's gave Rosinter Restaurant holding the subsidiary right to develop the chain in railway stations and airports in Moscow and St. Petersburg. So far only one McDonald's outlet was opened by Rosinter in St. Petersburg airport Pulkovo. McDonald's sales in Russia totaled \$2.2 billion (641.4 billion rubles) in 2013 or about 8 percent of its worldwide sales of \$28.1 billion.

On August 20, 2014 Federal Service for Supervision of Consumer Rights Protection and Human Welfare (Rospotrebnadzor) launched a campaign of sanitary checks at various McDonald's premises throughout the country, which resulted in 10-12 outlets being temporarily closed. The Russia's consumer watchdog stated that McDonald's products contain more fat, protein and carbohydrates than are allowed in Russia. The most recent closure of a McDonald's restaurant in Volgograd was as a result of it failing to reach Russian hygiene standards, including some of the products testing positive for E.coli bacteria. According to Business Insider, the company has stated that more than 200 of McDonald's restaurants in Russia are now under government investigation. Overall profits fell nearly 30 percent, according to McDonald's third quarter results report. McDonald's stated that it has lost 0.92 percent in diluted earnings in the third quarter of 2014 because of the temporary closures of the restaurants in Russia and Ukraine. McDonald's is planning to appeal the court decision on the closure of the restaurants at a higher judicial level. McDonald's same-store sales in Russia were "very weak" in November, as a number of the fast-food chain's outlets were closed this past summer after unscheduled checks by Russia's food safety watchdog. Many have reopened since. But, says the company, inspections are still proceeding and some restaurants remain closed after court decisions. Recently press-service noted that despite the claims made by Russia's consumer watchdog, McDonald's is planning to open about 40 new restaurants in 6 cities of Russia's Siberia. The McDonald's is about to develop the restaurant chain in Siberia. It plans to open new outlets in Novosibirsk, Tomsk, Omsk, Barnaul, Novokuznetsk and Kemerovo.

The group of top five players also includes Tomsk chain of ice cream cafes **33 Penguins** with 485 outlets. The Russian ice cream fast food chain 33 Penguins is seeing rapid growth based on its low start-up and operating costs (the only equipment needed is a refrigerator). Outlets are primarily located in retail locations and serve a quick, low-priced demand.

Baskin Robbins is somehow lagging behind the leaders with 327 chain eating places under this brand. Baskin Robbins, the world's largest chain of ice cream specialty shops, entered Russia in 1990. In 1996, the company opened a major ice cream plant in Moscow -- the biggest in Europe -- able to churn out 16,500 tons annually. The company sells more than 140 flavors of premium ice cream. In 2010, the company expanded its assortment range and increased the number of prepackaged ice-cream products offered at its outlets. The largest Baskin Robbins ice cream cafe in Europe opened in Moscow's Novyy Arbat in July 2011.

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

national traditions and preferences (traditional Russian meals - pancakes/crepes and baked potato) these chains have lost their shares of market pie to global players every year.

Impressive expansion and high marketing activity of **Burger King** forced Kroshka-Kartoshka off its market positions. Russian chain lost its fourth position to American chain in ratings of most well-known and well-attended fast food restaurants in Russia. Burger King has established a presence in Russia by opening its first restaurant in Moscow on January, 2010. Burger King is using its traditional franchising scheme to expand the chain in Russia. In order to launch operations in Russia, Burger King has established a daughter company Burger Rus, managed by Alexander Kolobov who has also successfully established a well-known coffee -shop chain called Shokoladnitsa. Under the terms of its franchise agreement, Shokoladnitsa is required to give 5 percent of its turnover to Burger King, while Burger King is obliged to pay for the opening of each restaurant. In June 2012, Burger King and the fast food giant's Russian franchisee Burger Rus established a joint venture with VTB Capital, the investment arm of Russia's second biggest lender, to develop and expand the restaurant's chain and brand presence in the country. Thanks to that partnership Burger King opened 58 new restaurants in Russia from July 2012 to July 2013, expanding its chain to 105 and opening the outlets all over the Russia, including Novosibirsk, third Russian city by population. Burger King doubled the number of its outlets from July 2013 to September 2014, demonstrating the highest fast food market developing growth in Russia. Currently there are 235 Burger King outlets in Russia, with 10 of them in the airports.

Russia has had the highest **KFC** store sales growth out of our 20 business units around the world. As of September, 2014 in Russia operate 290 KFC restaurants. According to recent surveys, the typical KFC customer is between 16 to 39 years of age, is not afraid to try new things and wants to see society progress while enjoying a Western dining experience. The average check at local KFCs amounts to 265 rubles per person.

2014 is one of the key years for development **Sbarro** in Russia, because the company launched the project of assortment standardization. Currently company operates 160 pizza restaurants with the average check of 290 rubles.

When choosing a fast food place 54 percent of Russians prefer McDonald's, which speaks for high customer loyalty. According to RBC research, impressive dynamics of McDonald's and strengthening of the brand helps to keep the gap between the chain and its closest rivals in terms of chain popularity. About 78 percent of Russians visited McDonald's at least once during first six months of 2014, meanwhile same index for KFC, Subway and Burger King constituted 47, 37 and 34 percent respectively.

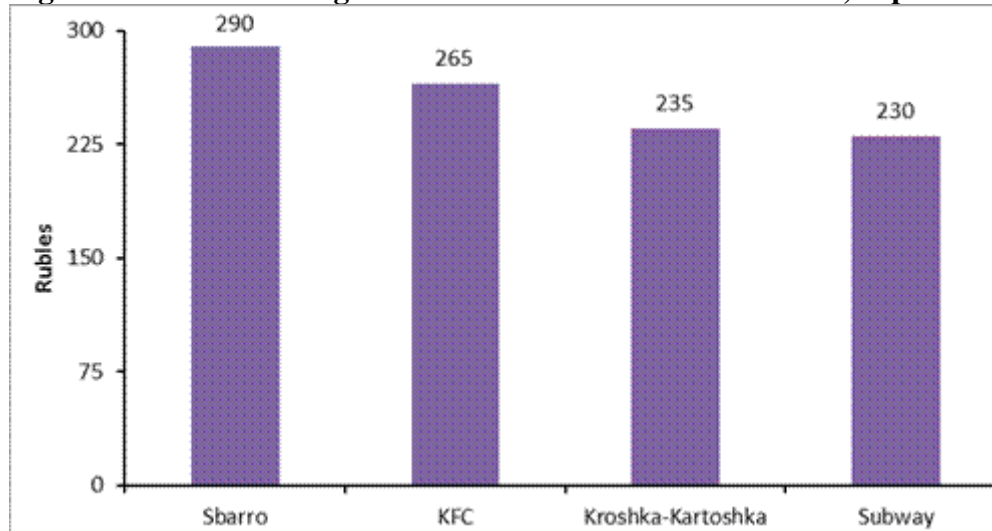
Table 10. Russia: Other USA Fast Food Restaurant Chains in Russia

Chain name	Country of origin	Year est. in Russia	# outlets, July 2014
Cinnabon	USA	2009	109
Papa John's	USA	2005	74
Carl's Junior	USA	2007	43
Dunkin Donuts	USA	1996/2010	32
Krispy Kreme	USA	September, 2013	4
Wetzel's Pretzels	USA	December, 2013	6
Nathan's Famous	USA	September, 2013	1

Source: Trade press, companies' web-sites

According to RBC research, the average check at fast food restaurants virtually unchanged last four years. On average, when visiting fast food establishments, Russians spend about 253 rubles.

Figure 7. Russia: Average Check in Some Fast Food Formats, September 2014



Source: Foodservice magazine of September 2014

Food ingredients substitution is not so critical for fast food, because restaurants tend to use a higher percentage of local ingredients (around 70-85 percent) as compared to other restaurants. This decision is driven by high turnover and the need for a consistent supply-chain more than by direct preference. Several fast-food chains have created internal supply-chains based in Russia. For example, McDonald's gets 85 percent of its menu items from 160 domestic suppliers.

Burger King restaurants in Russia get a significant share of their food from domestic suppliers. The company has about 40 suppliers in Russia, of which more than half are local producers. Since 2010 Marr Russia supplies frozen hamburgers to McDonald's, KFC, Burger King, and Carl's Jr. outlets. KFC works only with domestic suppliers. Recently Subway found substitution of imported cheeses and now works only with local ingredients as well.

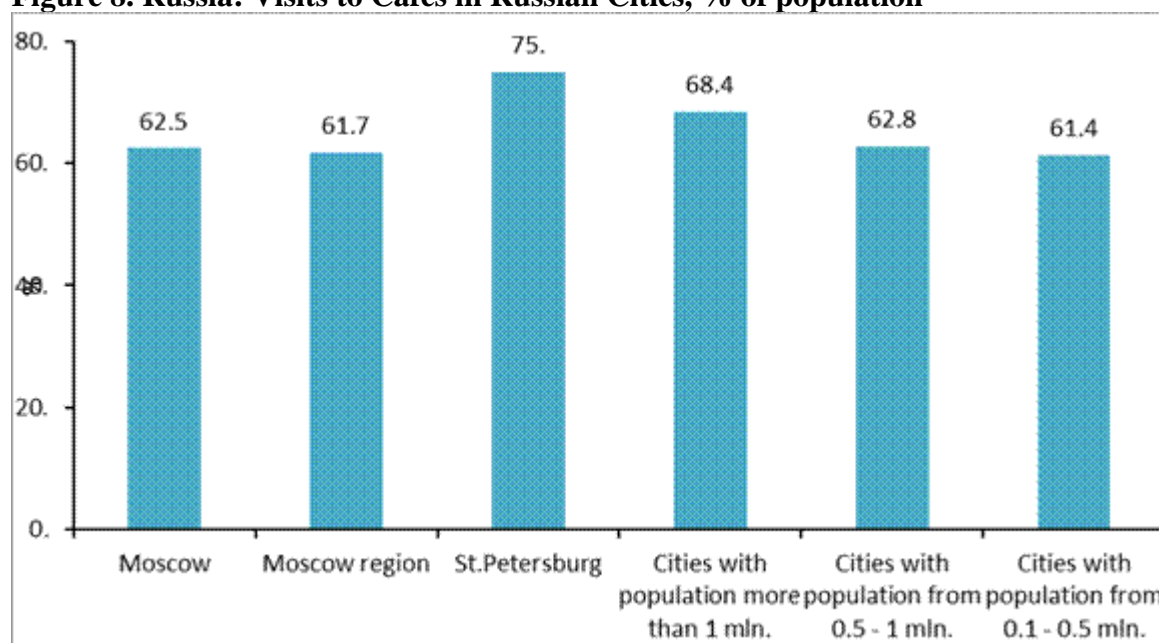
Major ingredient for pizza fast food format is cheese, so Pizza Hut, Domino's Pizza and Papa John's chains are trying to substitute cheese from banned country on local product. The Russian franchise operator of Papa John's, which has 74 outlets in the Russia, will probably freeze expansion plans due to the product inflation from the import ban.

Coffeehouses

The café market in Moscow and its suburbs is currently estimated to be worth about \$2 billion. The popularity of cafés among urban consumers in the largest Russian cities is large and growing. According to InFOLIO Research Group, the value of the café market reached 6.73 billion rubles in 2012 (14 percent increase in comparison to 2011). In 2012, chained specialist cafes in Russia registered an impressive 26 percent current value growth and a 16 percent increase in the number of outlets, riding a wave of interest in coffee culture, particularly among the urban affluent consumer.

Chained cafés/bars recorded current value growth of 47 percent in 2013 with sales reaching 34 billion rubles, while the number of outlets grew by 17 percent to reach over 1,700. This growth reflects the sharp development of chained foodservice players, which are mainly expanding regionally. In 2013, 18.1 percent of Russians went to cafes - making them second only to fast-food restaurants in popularity. That figure dropped to 13 percent in the first quarter of 2014, which has seen it outflanked by sushi bars and pizzerias, according to Synovate Comcon consultancy. Market analysts have stated that 65 percent of residents from 18 to 54 years of age from cities with a population of more than 100 thousand visited cafés in 2013.

Figure 8. Russia: Visits to Cafes in Russian Cities, % of population



Source: RBC Research

Currently there are roughly 5,200 cafés in Russia. About 1,340 of them are managed by 80 chain operators. Most cafés are concentrated in Moscow – about 670, and in St. Petersburg - about 470 coffeehouses. In Moscow each third café belongs to Shokoladnitsa and each fifth belongs to Coffee House. There is an increasingly high concentration of the leading chains, including Shokoladnitsa, Coffee House, Coffeeshop Company, Starbucks, McCafé, and Costa Coffee in these cities leading many of these chains to expand to the Russian regions. Non-chain cafés are significantly less common in the large cities. The rapid development of modern hypermarkets, trade centers, shopping malls, and business centers is helping leading chains, more so than independents, to enter regional markets.

Table 11. Russia: Market Share of Chained Café Leaders, in Percentage

Brand	Company name	2008	2009	2010	2011	2012	2013
Shokoladnitsa	Gallery Alex OOO	37.5	34.7	34.9	34.1	35.7	40.0
Coffee - House	Coffee House ZAO	33.3	31.7	29.3	26.7	25.2	23.6
Coffeeshop Company	Schärf Coffeeshop GmbH	0.9	2.5	4.0	8.8	10.8	12.5
Starbucks	Starbucks Corp	2.2	5.0	6.6	6.9	7.3	6.7
McCafe	McDonald's Corp	2.4	2.5	2.6	2.6	2.4	2.4

Costa Coffee	Whitbread Plc	1.6	2.2	2.8	2.8	2.3	2.2
Traveler's Coffee	Traveler's Coffee OOO	0.9	1.3	1.6	1.7	1.9	2.0
Others		22.2	20.1	18.2	16.4	14.4	10.6
Total		100	100	100	100	100	100

Source: Euromonitor

Regions are now becoming the main focus in expansion plans as Moscow and St. Petersburg are near the saturation levels of other major European cities in terms of chained cafés and independent cafés presence. Franchising is one of the main tools of coffee shops development, especially in the chained segment. The leading Russian café chain **Shokoladnitsa** has already opened outlets not only in Moscow (where there are around 250 establishments under the brand) and St. Petersburg, but also in Yekaterinburg, Volgograd, Kazan, Kemerovo, Novosibirsk, Sochi, Rostov-on-Don, Ufa, Tyumen and Chita, as well as abroad: in Yerevan, in Almaty and in three cities of Ukraine. Moreover, at the moment it focuses on regional expansion to the far eastern region of Russia. Shokoladnitsa brand chained outlets are franchised across Russia and have a strong brand identity with Russian consumers.

Two café chains leaders, Shokoladnitsa and Coffee House, together own about 600 outlets and have value shares of 7% and 5% respectively. Shokoladnitsa is closer to an Italian type café with a cozy interior while **Coffee House** is a more American-style coffee shop, with the décor being airy and uncomplicated. As a result, the clientele differs: Coffee House is preferred by consumers under 30 while Shokoladnitsa is favored by a more mature audience. Most of the Coffee House and Shokoladnitsa outlets are located in the food courts of new shopping malls and business centers. Prior to the acquisition Coffee House by Shokoladnitsa, Coffee House was investing heavily in chain development and incurring large debts. Shokoladnitsa's annual turnover is about \$300 million - excluding franchises. Approximate turnover of Coffee house is between \$160-170 million annually.

Locally-owned brand dominance is only likely to get stronger in the short-term as Shokoladnitsa's (Gallery Alex OOO) acquisition of number two player Coffee-House (Coffee House ZAO) this October. According to market analysts, estimated turnover of Shokoladnitsa may increase 1.5 times, exceeding \$450 million due to the merger. The owner of Shokoladnitsa, Russian restaurant mogul Alexander Kolobov, whose portfolio includes sushi chain Vabi Sabi, Burger King Russia and Israeli confectioner Max Brenner, is planning to develop the Shokoladnitsa brand instead of Coffee House in the future.

In 1997 Christopher Tara Browne, a former music producer from America, opened in Siberia a café called **Traveler's Coffee**, which began as a small counter inside of a pizza shop. Due to the popularity of its offerings, Traveler's Coffee has expanded substantially. Currently the Traveler's Coffee brand name is used in 67 cafés by franchises in different Russian cities including Moscow and St. Petersburg. The shop even has its own roaster in Novosibirsk, setting it apart from many coffee shops, by giving it a higher degree of customization and roast control.

Foreign coffee chains and other western franchises face an increasingly difficult operating environment for their brands and the franchise businesses of local players. In 2007, two leading multinational coffee shop chains appeared on the Russian market, adopting different development strategies. The world leader, **Starbucks** Coffee Company, opened its first outlet in Moscow in September 2007. In December 2012, Starbucks finally opened its first café in St. Petersburg and currently operates 75 coffee shops in

Russia, 63 of which are in the capital. The company is planning to enter Yekaterinburg and Tyumen in 2015 seeking to expand Starbucks' Russian footprint beyond major cosmopolitan centers. In October 2014, **Costa Coffee** (Whitbread Plc) chain in Russia - through local franchise partner Rosinter Restaurants Holding - announced plans to aggressively expand beyond the Moscow market. The company now plans to focus their Costa Coffee locations in alternative urban markets in Russia.

Austrian chain **Coffeeshop Company** has operated in Russia since 2008 and currently is number three by coffee sales after Shokoladnitsa and Coffee House. Russia is among the company's largest export markets and is growing rapidly. 82 coffee shops have been established in Russia with about half of them in St. Petersburg. In 2014, the owner of the Austrian company Schärf Coffeeshop GmbH, owner of the Coffeeshop Company chain, became minority shareholder of a Russian company called "Coffee SET". The deal amounted to a 2 million euro investment which will be used to expand Coffeeshop Company cafés in Russia. For comparison, 293 outlets operate all over the world, 38 of which are located in Austria. The appearance of these leading multinational coffee chains in the Russian market has changed the position of the coffee shop segment.

Table 12. Russia: Leading Coffeehouse Chains in Russia

Chain Name	First Year of Operation	# Outlets July, 2013	# Outlets July, 2014	% Growth Year-on-Year
Shokoladnitsa	2001	361	403	11.6
Coffee House	1999	209	182	-13
Coffeeshop Company	2008	73	82	12.3
Traveler's Coffee	1997	67	77	14.9
Starbucks	2007	64	75	17.1
McCafe	2002	57	60	5.2
Costa Coffee	2007	28	30	7.1

Source: Restaurateur magazine, Foodservice magazine, trade press

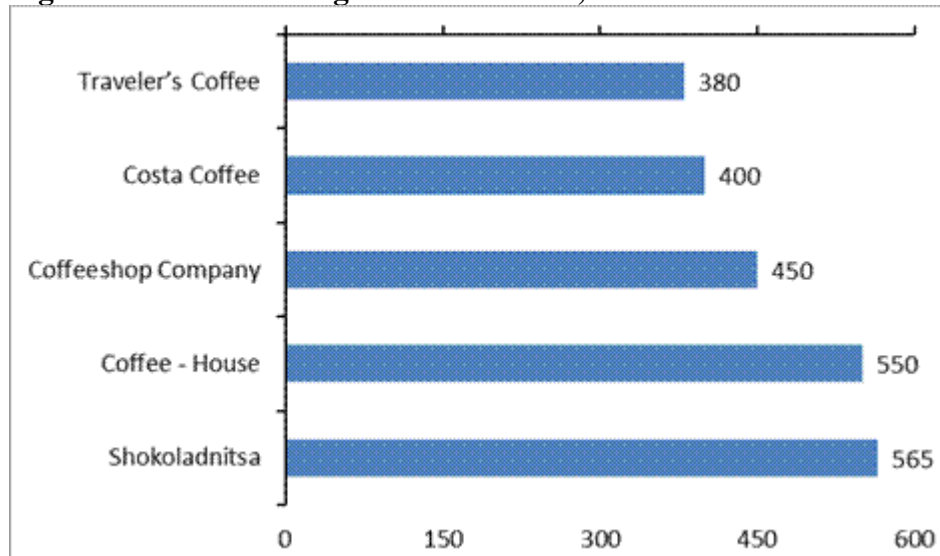
Table 13. Russia: Outlets of Leading Coffeehouses Chains in Moscow & St. Petersburg

Chain Name	Country of Origin	# Outlets in Moscow	# Outlets in St. Petersburg	Web-sites
Shokoladnitsa	Russia	257	31	www.shoko.ru
Coffee - House	Russia	108	65	www.coffeehouse.ru
Coffeeshop Company	Austria	19	37	www.coffeeshopcompany.ru
Traveler's Coffee	Russia	2	1	www.travelerscoffee.ru
Starbucks	USA	63	6	www.starbucks.com
McCafe	USA	28	11	www.mcdonalds.com
Costa Coffee	Great Britain	23	3	www.costa.co.uk

Source: Foodservice magazine July 2014, trade press

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

Figure 9. Russia: Average Check in Cafés, in Rubles



Source: Foodservice magazine of 2014

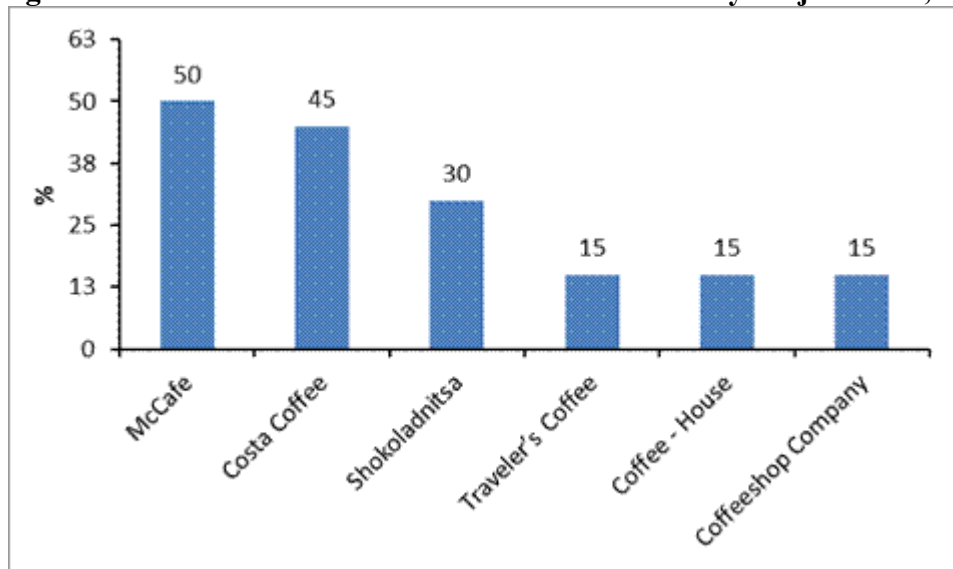
Russian coffee shops that sell a variety of desserts and confectionery products have created a new and interesting market for U.S. exporters of desserts, nuts, ingredients, and dried fruit. Traditionally, Russians have been large tea consumers going back several generations. But in the last decade, per capita coffee consumption has rapidly increased – by 4 times in 2012 compared to the level of 2000, when only 68 million people in the country regularly consumed coffee. In 2014, this figure, according to numerous forecasts, will rise to 94 million people accounting for more than 60 percent of the Russian population.

Market analysts have noted that Russian coffee consumption is forecast to grow by 4 percent in volume terms in 2014 as its popularity continues to increase. Leading market players are actively marketing coffee to the under 30 age group and increasing the numbers of cafés in Russia while at the same time facilitating a growing “to go” coffee culture. Consumers are also becoming more aware and educated about the coffee they drink. They know that homemade coffee is considerably different (usually worse) from what cafes or restaurants serve. This depends not only on the barista’s skills but also on the variety of coffee being used.

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

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

Figure 10. Russia: Share of Sales of “To Go” Coffee by Major Cafés, in Percentage



Source: Foodservice magazine of 2014

Hotel Sector SnapShot

Investment in hotels in Russia has been very attractive in recent years driven by limited supply of quality lodging facilities, low overall competition, gradually improving business climate, and growing domestic and foreign travel volumes. One of the recent trends is the growth of hotels in regional cities of Russia due mainly attributable to the large-scale international events taking place in Russia such as the UPEC Summit in Vladivostok in 2013, World Summer University sport games in Kazan in 2013, Winter Olympics in Sochi in 2014, Race Formula 1 in Sochi in 2014, and FIFA World Cup in Russia in 2018. Before the recent devaluation of the Russian ruble and news of contracting economic indicators were announced, it was estimated that by 2017, the number of hotels under international management will increase by 157 new operators (32,000 rooms). If true, the number of hotels under international management in Russia will amount to 257 hotels (56,825 rooms) located in more than 50 Russian towns and cities.

According to Russia's State Statistics Service (Rosstat), Russia had 9316 functioning hotels able to accommodate 618,000 guests at the beginning of 2013. Almost 7 percent (40,058) of hotel rooms are in Moscow, 16 percent (91,681) are in Russia's popular Black Sea resort area Sochi, and 4.5 percent (25,370) are in St. Petersburg.

Table 14. Russia: Hotel Industry Sales in Russia, 2009-2013

	2009	2010	2011	2012	2013
RUR, billions	98.3	115.6	137.2	161.8	260
Growth Year on Year, %		17.6	18.7	17.9	60.7
Average exchange rates by years	31.72	30.36	29.35	31.07	31.82
Number of hotels in Russia	6774	7410	7866	8406	9316

Source: Federal State Statistics Service

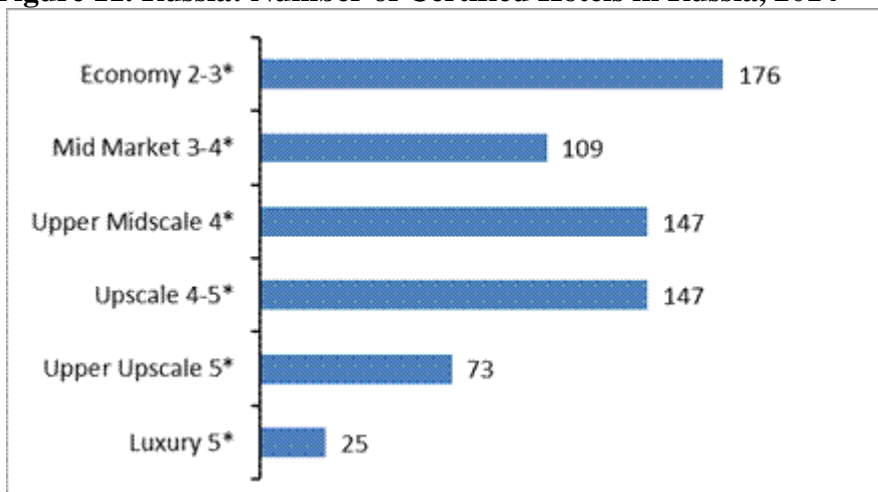
More than 50 new hotels under western brands have been built across Russia in 2014 with many in St. Petersburg and major regional capitals. More than 11,100 rooms will be opened in new international hotels across the Russia by the end of 2014. Hilton Worldwide is the most active on Russian hotel market and has opened more than 3,000 rooms this year.

Market analysts have stated that roughly 28 million foreign tourists visited Russia in 2013 with the vast majority heading for Saint-Petersburg (90 percent of this amount). In 2014, the tourist flow to Russia reduced by 30-50 percent compared to 2013 due mostly to the tensions in the region. As a result, profitability of Moscow Western style hotels in the first 3 quarters of 2014 fell by 18 percent in dollars compared with the same period last year. Profitability of St. Petersburg hotels fell only on 9.5 percent for the same period due to high tourist interest to the city.

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

Luxury hotels represent the best opportunity for selling American products to hotels. Other sub-categories usually have very limited foodservice offerings. Hotel restaurants operate like other restaurants and purchase items through distributors. American meat, fish, wine, spirits, and fruit are some of the better prospects for this segment.

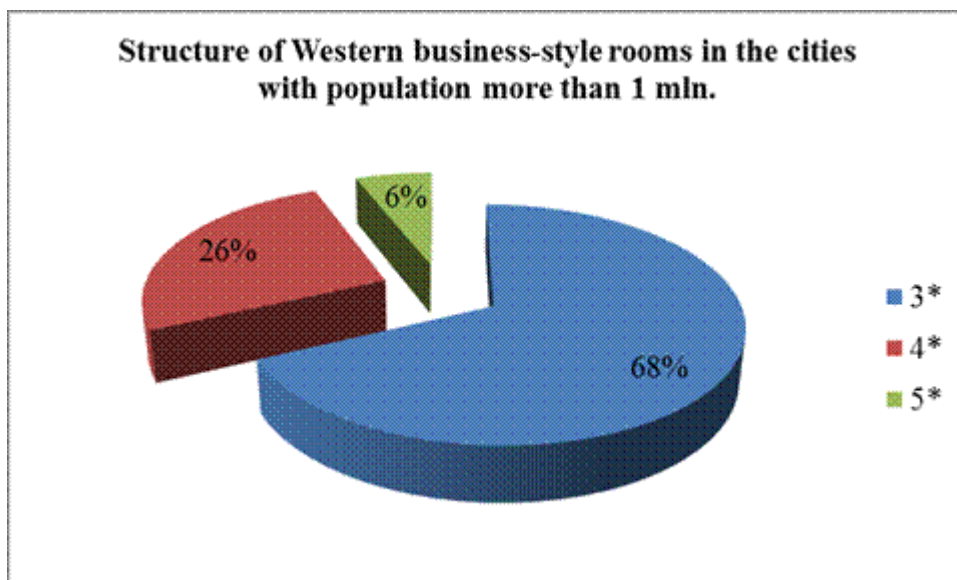
Figure 11. Russia: Number of Certified Hotels in Russia, 2014



Source: STR Global

Russia's hotel industry is facing a room shortage. GVA Sawyer estimates that there are currently only 55,000 Western business-style hotel rooms available. In fact, most existing three, four and five-star hotels in Moscow and St. Petersburg were built during the last decade. As a result, Moscow currently has 20,800 Western business-style hotel rooms, and St. Petersburg has 15,530.

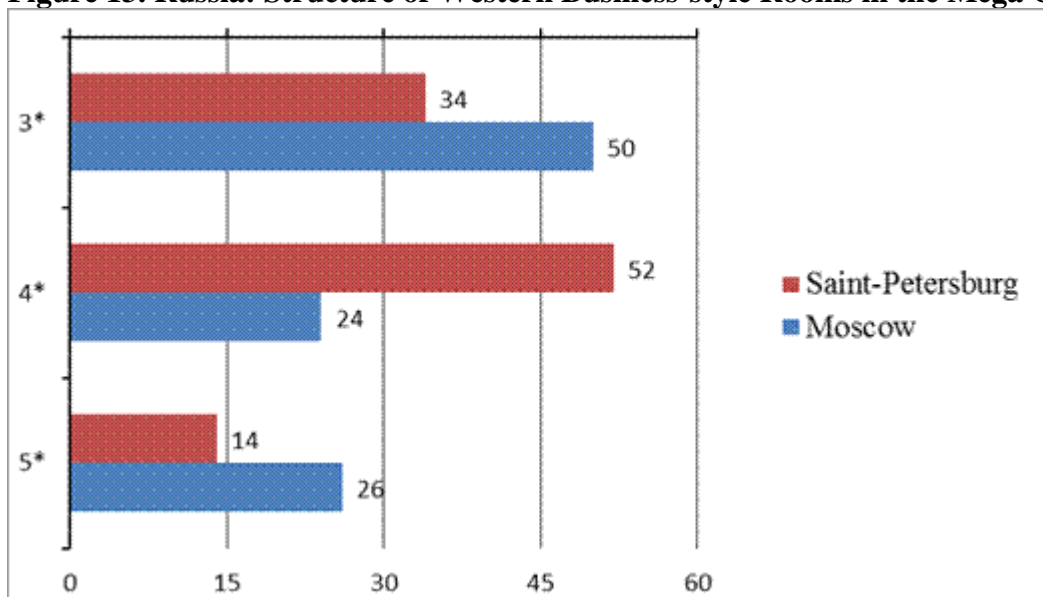
Figure 12. Russia: Structure of Western Style Rooms



Source: GVA Sawyer, 2013

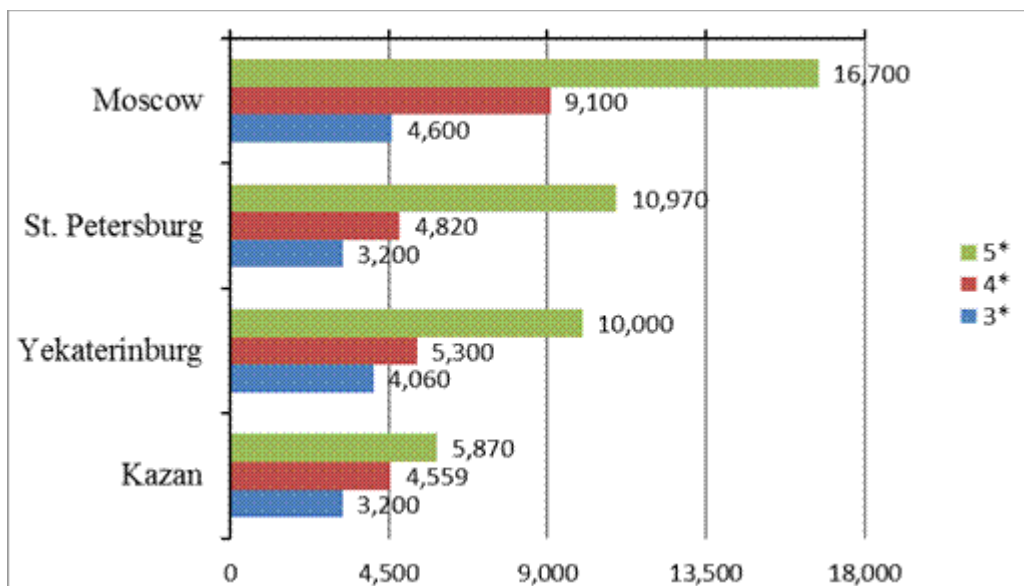
Moscow is one of the largest cities in Europe and remains the country's main city for hotel development. According to Federal State Statistics Bureau as of the end 2014 about 230 hotels were operating in Moscow with approximately 105,000 rooms, 30 percent of which are 5 and 4 stars hotels.

Figure 13. Russia: Structure of Western Business-style Rooms in the Mega Cities, %, 2014



Source: GVA Sawyer, Industry Data, Cushman & Wakefield

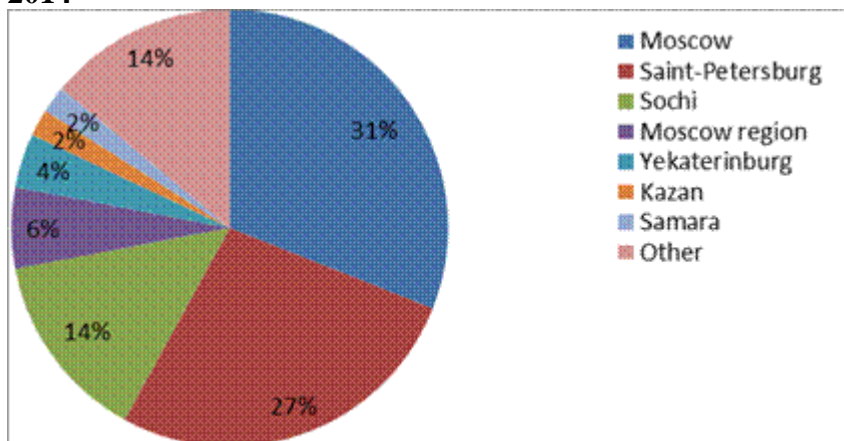
Figure 14. Russia: Cost Per Room Per Night in 2013, Rubles



Source: GVA Sawyer

Since 1991 Russia has seen the emergence of more international brands and there remains further opportunity for investment in the hotel sector across all categories. Moscow and St Petersburg alone account for around 25 percent of the country's hotel capacity. While the high-end sector is close to saturation, there is a strong demand for midlevel hotel rooms. The highest level of unfulfilled demand is for quality three star and economy hotels.

Figure 15. Russia: Current Room Supply with International Brands in Russian Regions, June 2014

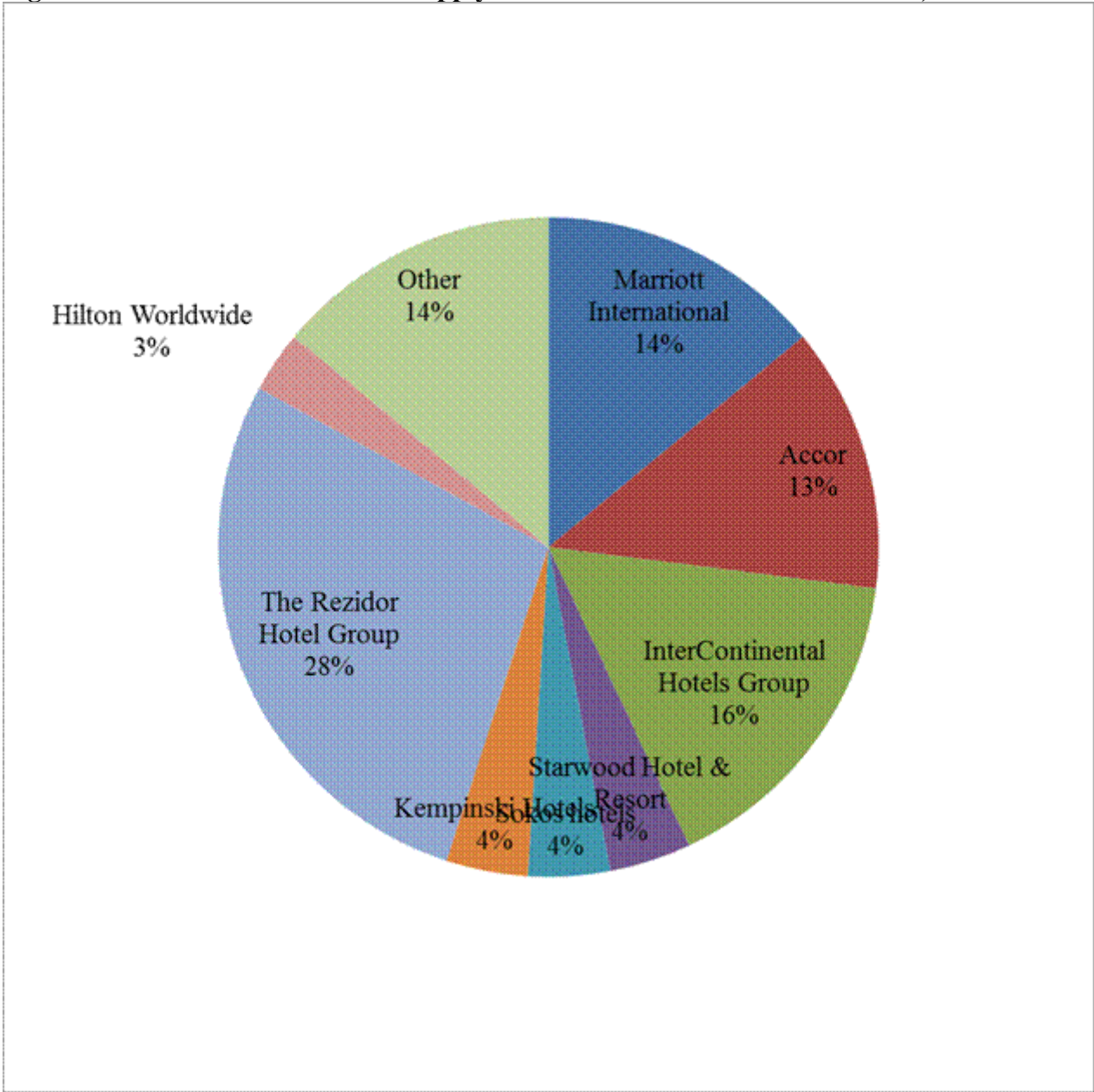


Source: Ernst & Young (CIS) B.V.

The regions outside of Moscow and St. Petersburg represent a small fraction of the travel industry, but some areas such as Sochi, Rostov-on-Don and Vladivostok are growing quickly. Yekaterinburg, Novosibirsk, Nizhny Novgorod, Krasnoyarsk, Kaliningrad, and Kazan are other regions where travel and tourism are growing, particularly for business travel. International operators, such as Hilton Worldwide, the Rezidor Hotel Group, Marriott International, and Accor have built two-three new hotels in cities with populations over one million in the last five years. Major hotel chains are opening

facilities in the regions. The Rezidor Hotel Group (including Radisson and Park Inn brands) is currently targeting some 35 key cities in Russia with a population of 500,000 and above to further develop its portfolio of hotels and brands.

Figure 16. Russia: Current Room Supply with International Brands in Russia, 2014



Source: Ernst & Young (CIS) B.V.

Table 15. Russia: International Hotel Brands in Russia 2014

Hotel Operator	Hotel Brands	Locations	First year of operation in Russia	Opening in 2014
Fairmont-Raffles Hotels International	Swissotel	Moscow Kazan Sochi	2005	
Marriott International	Marriott Courtyard Ritz Carlton Renaissance	Moscow Samara St. Petersburg Irkutsk Kazan Krasnodar Krasnoyarsk Novosibirsk Omsk Voronezh	1991	1009
Hyatt Hotels Corporation	Ararat Park Hyatt Hyatt Regency	Moscow Yekaterinburg Rostov on Don Vladivostok	2002	660
InterContinental Hotels Group	Crown Plaza InterContinental Holiday Inn	Moscow Samara Chelyabinsk St. Petersburg Naberezhnye Chelny Samara Voronezh	1998	786
Starwood Hotel & Resort	Sheraton	Moscow Kaluga Rostov on Don	1997	479
Best Western International	Art-Hotel 4*	Moscow St.Petersburg	2005	
Kempinski Hotels	Kempinski	Moscow St.Petersburg Gelendzhik	1992	
Accor Group	Novotel Mercure Ibis	Moscow St.Petersburg Yekaterinburg Sochi Nizhniy Novgorod Kaliningrad Kazan Samara Omsk Yaroslavl Lipetsk Rostov on Don Tyumen	1992	871
The Rezidor Hotel Group	Radisson Park Inn	Moscow Sochi St.Petersburg Kaliningrad Rostov on Don	1991	2251

		Astrakhan Yekaterinburg Izhevsk Kazan Murmansk Velikiy Novgorod Chelyabinsk Lipetsk Nizhniy Novgorod Novokuznetsk Novosibirsk Sochi Volgograd Voronezh		
Small Luxury Hotels of the World	Savoy	Moscow	2003	
Hilton Worldwide	Hilton Hilton Garden Inn Double Tree by Hilton	Moscow Krasnodar Perm Novosibirsk Kaluga Samara Kirov Krasnoyarsk Omsk Perm Sochi St.Petersburg Volgograd Yaroslavl	1997	3142
Four Seasons Hotels & Resort	Four Seasons	St. Petersburg Moscow	2013	180

Source: Industry Data, Ernst & Young (CIS) B.V.

In 2013, 16 hotels managed by international operators were opened in Sochi before the XXII Sochi Winter Olympic Games on February 7-23, 2014, and the XI Winter Para Olympic Games on March 7-16, 2014. In 2013, Four Seasons opened its first Russian hotel, transforming a 19th-century palace apartment building in St. Petersburg. Second Four Seasons Hotel was opened near Moscow Kremlin this October.

Cities highlighted by green color in the table above show where the hotels have opened in 2014. Hotel projects usually have a four to five-year development cycle, so international hotel operators are building hotels before upcoming events in the Russian regional centers. The following events are planned for the near future: the 16th FINA World Championships in Kazan from 24 July to 9 August 2015 and the 2018 FIFA World Cup. Matches are to be held in 11 cities, including Moscow, St. Petersburg, Kaliningrad, Kazan, Yaroslavl, Nizhny Novgorod, Samara, Saransk, Rostov-on-Don, Volgograd, and Sochi. According to the requirements of FIFA World Cup, an increase of the hotel room capacity is needed in selected cities in order to host the World Cup. 2015 World Aquatics Championship competitions will be held in facilities built for 2013 Summer Universiade, also hosted by Kazan. Ten thousand hotel beds, including hotels with western brands, are available in Kazan now.

Institutions

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

Table 16. Catering Market in Moscow

	2012	2013
Market volume, mln. rubles	2,112	2,365
Annual growth, %	10	12

Source: Catering Service Company

According to expert estimates Moscow catering market will show only 6 percent growths in 2014. 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. Russia's leading caterers are Sodexho, Mega Foods, Parad Catering, Brizol, and Master Foods which have total market share of about 50 percent of catering services.

The Russian catering market consists of several segments, each of which has a different service audience, number of players, average bill per person, and profit, including:

- Lunch deliveries;
- Corporate catering; and
- Off-premise catering.

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

Office cafeterias form another changing segment. Until recently, most cafeterias operated in the Soviet fashion, offering few choices and low quality. As incomes growth, the office cafeteria is transforming. Corporate catering firms manage stationary foodservice facilities, placing them in office buildings, business parks, shopping centers, administrative complexes, and industrial facilities. Their goal is to give people high quality meals in these institutions on a daily basis. The average bill in office cafeterias is \$7 to \$9. Newer cafeterias are beginning to use higher quality ingredients. They still prefer to buy whole, non-processed items, and they are very price sensitive. Like many restaurants, they monitor prices weekly and do not hesitate to change suppliers or menus if they encounter a better price.

Catering for private events and parties, especially those in the premium segment is another attractive and profitable area of foodservice. Restaurateurs and five-star hotels are rushing to enter this lucrative market, including Gurme Catering, Baltschug Kempinski, and Swissôtel Krasnye Holmy. Their teams of culinary professionals are willing and able to delight customers. Hotels are attractive caterers because they are flexible enough to deliver a five-star experience in any venue, and they have an extensive wine

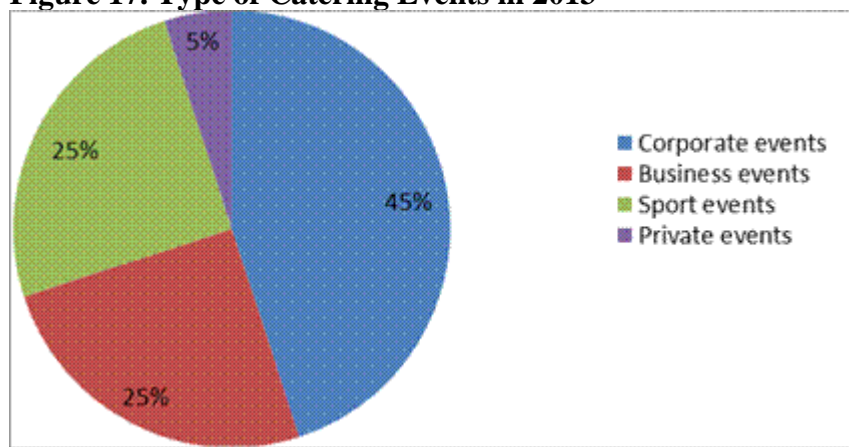
knowledge. The average bill for mid-level off-premise catering is \$50 per person, but prices can be significantly higher in the premium class.

Table 17. Moscow Catering Segments

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

Source: Catering Service Company

Figure 17. Type of Catering Events in 2013



Source: Catering Service Company

Caterers use many categories to tailor their products to the client, and they usually work with the same distributors as restaurants. Like restaurants, caterers use a variety of distributors and suppliers depending on their needs. Mid-level and high-end caterers import a variety of food, presenting an attractive opportunity for U.S. products. There is a particular demand for specialty items such as seafood, meat, wine, and nuts.

While there is not yet a national school lunch program in Russia, there is interest in creating one. The Russian government is studying the U.S. government program and will no doubt incorporate some of its elements to improve the school lunch program in Russia. Packaged 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 military could be other potential customers for catering companies, but tenders are often not competitively bid for catering contracts with government institutions.

In 2008, Russian Railways created the joint venture Yedinaya Set Pitaniya with RP-Com, one of the top 20 foodservice operators in Moscow. This enterprise manufactures ready meals for passengers of the Russian high-speed railways, which currently operates on three lines: Moscow-St. Petersburg, Moscow-Nizhny Novgorod and St. Petersburg-Helsinki. By the end of 2010, the company produced 20,000 meal

trays per day from its first catering facility near St. Petersburg. Other catering facilities have built in Yekaterinburg, Novosibirsk, Sochi, and Rostov-on-Don. According to RF Government plan, 8 Russian cities hosting 2018 World Cup matches should be linked by an integrated high-speed rail network.

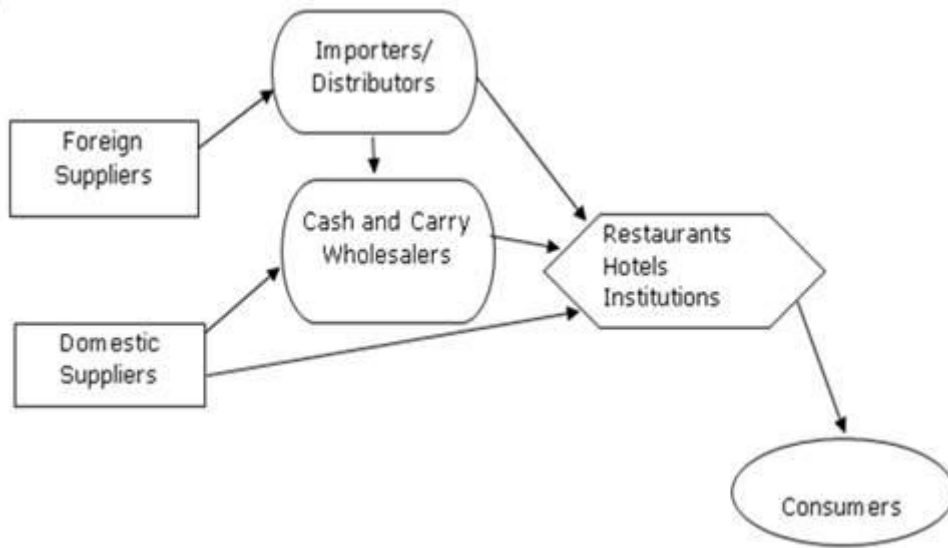
Operators at the major airports in Moscow and St. Petersburg usually function more as part of a restaurant chain than as an institutional operator. According to airport statistics, 30 to 40 percent of passengers eat in airports. Leading Russian foodservice operator Rosinter has opened and operated restaurants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

The volume of air passenger traffic in Russia was about 85 million in 2013 (about 95 million passengers in 2014). The volume of passenger traffic through Moscow's two main airports, Domodedovo and Sheremetyevo, exceeded 60 million passengers in 2013 (10 percent increase). Airlines contract with professional catering companies for in-flight meals for passengers. JSC Domodedovo Air Service is the largest Russian company serving up to 60,000 in-flight meals and rations per day in Domodedovo airport. AeroMar has provided in-flight catering services to the passengers of Sheremetyevo airport since 1990.

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

SECTION II: ROAD MAP FOR MARKET ENTRY

Figure 18. Distribution Channels for HRI Products in the Russian Market



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

Table 18. Russia: Advantages and Challenges for U.S. Exporters

<i>Advantages</i>	<i>Challenges</i>
Paying in Dollars is advantageous for exporting to Russia compared to Europe due to the lower cost of the Dollar relative to the Euro.	Ruble/\$ exchange rate has led to an increase in the price of U.S. products, mitigating some of the positive effects of the advantage over the Euro.
Russia's 143 million people make it one of the largest consumer markets in Europe.	Official government opposition to growth in food imports. The relatively low purchasing power of many Russian consumers, particularly in the regions.
Rising disposable incomes in the long term will allow Russians to spend more on food and beverages.	Economic vulnerability, dependence on oil and mineral extraction for most wealth.
Existence of large importers experienced in importing food products to Russia.	Competition with food products imported from EU and other countries may rise.
U.S. products have a reputation for consistency and high quality.	Logistics can be difficult. There are often long shipping times from the U.S., the major Russian port in St. Petersburg operates slowly and there can be complex customs regulations.

The HRI sector has a lot of room for growth. Restaurant chains are expanding out of Moscow and St. Petersburg to other cities with populations over one million.	Customers are very price sensitive. Food sanction has negative effect on trade.
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Entry Strategy

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

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

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

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

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

Provide Product Education: Marketing and product education are essential. Many of the HRI industry personnel are interested in new products, but they want to be shown how to use them and how the

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

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

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

Food Suppliers for the HRI sector

Very few HRI businesses operate on exclusive contracts with vendors. Most chain and independent restaurants change suppliers frequently, particularly if there is a price difference. Most businesses use a separate supplier for each product category (i.e. produce, meat, or desserts) and very often work simultaneously with three to four suppliers of their principal ingredients to ensure steady supply.

Whole foods are preferred and account for 70 percent of sales, principally because labor costs are low. Smaller restaurants without adequate space are usually the customers for semi-prepared items. Even fast-food chains tend to buy whole products and prepare them at the restaurant level. Exceptions to this include meat patties and French fries.

Few restaurants use fresh produce markets as suppliers. In contrast to U.S.-style produce markets, Russian markets have inconsistent supplies and offer goods of questionable quality. Markets also tend to have higher prices than other supply options.

There are a large number of importers and distributors in the HRI sector, both large and small. A few work across a wide variety of products, but many specialize in a particular category. The distribution market is fragmented, and there are a variety of arrangements between suppliers and customers. As noted above, imports make up the vast majority of HRI products (more than 65 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 2001. The company currently has 72 stores in 45

Russian regions, including twelve in Moscow and three in St. Petersburg. Foodservice operators across Russia have bought food, beverages, and other restaurant equipment from Metro Cash & Carry outlets. A reported Russian Metro Cash & Carry sale increased by 11.3 percent in 2013 and accounted 183.22 billion rubles.

Table 19. Russia's Major Suppliers of Food Products for Restaurants

Company	Principal Products	Customers	Locations
East-West	Marbled Beef	Restaurants	Moscow
	Veal	Hotels	St. Petersburg
	Beef		Krasnodar
	Pork		Novosibirsk
	Lamb		Yekaterinburg
	Fish and Seafood		
	Poultry		
	Groceries		
Global Foods	Marbled Beef	Restaurants	Moscow
	Veal	Hotels	St. Petersburg
	Beef		Krasnodar
	Pork		Yekaterinburg
	Lamb		Vladimir
	Poultry		Kremia
	Fish and Seafood		
	Groceries		
Australian Trade House	Marbled Beef	Restaurants	Moscow
	Veal	Supermarkets	
	Beef	Hotels	
	Lamb		
	Fish and Seafood		
	Butter		
Marr Russia	Marbled Beef	Restaurants	Moscow
	Beef	Supermarkets	St. Petersburg
	Veal	Hotels	Rostov-on-Don
	Lamb		
	Pork		
	Poultry		
	Fish and Seafood		
	Groceries		
Meridian	Marbled Beef	Restaurants	Moscow
	Veal	Supermarkets	St. Petersburg
	Groceries		
Miratorg	Marbled Beef	Restaurants	Moscow
	Veal	Supermarkets	St. Petersburg
	Pork		Regions
Snow World	Veal	Restaurants	Moscow
	Beef	Hotels	

	Pork		
	Lamb		
	Poultry		
	Fish and Seafood		
	Groceries		

Source: Industry data

Major suppliers of food products for the HRI sector have their offices in Moscow and St. Petersburg, Russia's primary restaurant markets. These offices handle foodservice-product imports and supply other Russian regions. 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 dependent 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 United States to Vladivostok.

SECTION III. COMPETITION

Russia imported approximately \$39.2 billion of agricultural products in 2013, according to Global Trade Atlas/Federal Customs Service. Year-on-year Russian agricultural imports can be seen in the following table:

Table 20. Russia: Growth in Agricultural Imports

	2009	2010	2011	2012	2013
Agricultural Imports, billion dollars ¹	27.6	32.9	38.9	38.1	39.2
Growth Year-on-Year, %		19.2	18.2	-2.25	2.85
5-Year Average Annual Growth Rate, %					9.5

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

Source: Global Trade Atlas/Federal Customs Service

Russia imported 2.85 percent more food products in 2013 compared to previous year, the Federal Customs Service reported. Imports of fresh vegetables rose 13.1 percent, dairy products – up 24.24 percent. Poultry meat import declined 5.51 percent, pork down 14.93 percent in 2013.

Table 21. Russia: Imports of Selected Foods from the World, millions of US dollars

Product	HS Code	2011	2012	2013	% change 2013/2012
Fresh & Chilled Beef	0201	199.98	218.55	212.87	-2.6
Frozen Beef	0202	2217.05	2583.31	2339.10	-9.45
Pork	0203	2108.70	2406.65	2047.37	-14.93

Poultry	0207	572.07	706.81	667.85	-5.51
Lamb	0204	45.73	51.31	55.99	9.14
Fish and Seafood	03	2360.23	2381.79	2767.25	18.87
Dairy Products		2117.93	2037.16	2531.57	24.24
Fresh vegetables	07	3062.84	2433.57	2752.49	13.10
Edible fruit and nuts	08	6093.42	6197.18	6266.31	1.12
Spirits	2208	1142.10	1399.60	1392.05	-0.54
Wine	2204	953.52	1052.06	1218.67	15.84

Source: Global Trade Atlas/Federal Customs Service

The Russian Federation is among the top export destinations for U.S. agricultural products. Based on official Federal Customs Service data, the U.S. share of agricultural products includes (HS codes 01 to 24) exceeded \$1.67 billion in 2013 (drop 18.55 percent). The U.S. share of Russia's agricultural imports in 2013 was 4.26 percent. According to BICO in January-October of 2014 U.S. share of Russia's agricultural products imports was \$799 million (-13 percent compare to Jan-Oct of 2013) because of the ban on U.S. meat since February 2012 and Russian food sanctions since August 2014.

Poultry have dominated U.S. agricultural exports to Russia followed by tree nuts, fish and seafood, spirits and wine. U.S. poultry exports to Russia in 2013 accounted for roughly \$310 million. U.S. poultry exports to Russia in the first 10 months of 2014 were \$ 150.34 million (down 43 percent).

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

According to President Putin's decree on August 6, 2014 all imports of meat, fish, fruit, vegetables, milk, and milk products from the U.S, as well as the European Union, Australia, Norway, and Canada are no longer allowed into the country. According to signed decree the ban will be valid for one year. Below is a link to report, courtesy (unofficial) translation of the decree signed by Russian President Vladimir Putin and list of agricultural products included in the ban.

[Russia Announces Ban on Many US Agricultural Products 2014](#)

Russia imported \$15.8 billion in food from the EU in 2013 alone, and the U.S sent around \$1.3 billion in food shipments last year. According to Federal Customs Services the banned items amounted to \$8.3 billion in 2013. Most of the affected imports came from Europe. The United States accounted for about \$670 million in 2013.

Table 22. Russia: Import of Banned Products, 2013

Banned Product	Total Import from Australia, Canada, EU, Norway, USA		% from Total Import
	Thousand tons	\$ million	
Beef fresh and chilled	16,23	49,32	26.2
Beef frozen	42,82	165,56	6.8
Pork fresh, chilled or frozen	450,79	1569,86	73.5

Poultry	338,73	432,39	51
Fish and Seafood	457,19	1553,77	54.3
Milk and dairy products	428,79	1786,37	42.8
Vegetables	914,73	944,65	32.8
Fruit and nuts	1599,57	1756,28	27.4
Sausages and products from meat	17,81	77,51	40.2

Source: Federal Customs Service, RBC

Table 23. Russia: Import Competition for Banned Products, 2013

Product	Country of Origin with the share from total import, %
Beef	Brazil-56%, Paraguay-26%, Uruguay-7%, Australia-5%
Pork	Brazil-21%, Denmark-15%, Germany-14%, Canada-14%
Poultry	USA-60% , Brazil-12%, Ukraine-9% , France-4%
Fish and Seafood	Norway-33% , Iceland-17%, China-9%, Faroe Islands-8%, Chili-6%
Cheese	Netherlands-17% , Ukraine-15% , Germany-12% , Finland-11% , Lithuania-11%
Vegetables	Turkey-16%, China-15%, Poland-11% , Netherlands-10% , Israel-9%
Fruits & Nuts	Ecuador-21%, Poland-13% , China-12%, Turkey-5%, Spain-4% , Egypt-4%

Source: Federal Customs Service

This is extremely difficult situations for the fine dining and even mid-range restaurant which serves sushi, seafood and have European menus. There are no substitutions for some of the banned products, such as American lobsters, Italian parmesan, and French oysters. Restaurant's suppliers are trying to find new exporters and selling the rest products from the storage.

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

Table 24. New Geography of Food Suppliers for HRI Sector

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

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

Source: Foodservice magazine of September 2014, importers

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

Many of the Russian restaurants have been hit hard because they get from 15 percent to 80 percent of their ingredients from sanctioned countries. Depending on restaurant specialization HRI sector is looking for replacement of banned products. Companies, which work in fine dining segment and event catering, are mostly depended on imported food, so the product ban mostly affected restaurants belonging to the higher price category. While the HRI sector uses mostly imported products, some ingredients are purchased domestically. These include root vegetables, such as carrots and beets, and other basic vegetables like cabbage and potato. Currently HRI sector is trying to use local products as much as possible and find appropriate food product substitution.

SECTION IV. BEST PRODUCT PROSPECTS

Interest in new product categories is growing. American products are consequently competitive and attractive to Russian importers. Currently importers are trying to find analogous to U.S. food products because of Russian food sanctions. Table 25 shows Russian imports of selected U.S. food products.

Table 25. Russia: Russian Imports of Selected Food from the U.S., millions of US Dollars

Product	Calendar Years (January-December)			January-October		
	2011	2012	2013	2013	2014	% change
Poultry	248.8	309.7	310.2	265.4	150.3	-43.3
Beef	249.5	298.6	1.0	0.9	0.6	-39.5
Pork	217.0	267.8	17.6	17.6	137.0	679.8
Tree Nuts	90.5	124.0	171.6	142.2	69.5	-51.2
Fish and Seafood	60.4	47.5	83.0	70.3	44.5	-36.6
Fresh Fruit	28.1	21.8	34.2	20.7	8.7	-57.8

Source: U.S. Census Bureau Trade Data/BICO

The U.S. is one of the world's leaders in developing the hospitality industry. U.S. producers can offer a wide range of products developed, manufactured, and packaged for the HRI sector.

Several product categories are particularly attractive for export to Russia. Fresh and frozen seafood, frozen and chilled high-quality beef, pork, cheese, fruit and tree nuts are in demand.

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

preparation products.

Wines and spirits also have high potential, but there is a lack of awareness about American wines.

Table 26. Russia: Imports of Alcohol Beverages from the U.S., millions of US Dollars

Product	Calendar Years (Jan-Dec)			% change 2013/2012	% market share
	2011	2012	2013		
Spirits	53.99	69.16	83.03	20.06	5.96
Puerto Rico (U.S.) rum	35.23	34.93	40.99	17.36	2.95
Wine	9.69	12.34	15.68	27.03	1.29
Beer	0	0	0.06		0.03

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

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For Trade Policy/Market Access Issues,

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USDA Stakeholders

The Agricultural Trade office works with a large number of U.S. industry organizations, several of which are resident in Russia. These cooperators share the view that Russia is a promising market for food products.

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USA Dry Pea and Lentil Council

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Email: office@rkmarketing.ru

USA Poultry and Egg Export Council (USAPEEC)

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

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<http://www.usapeec.ru>

U.S. Meat Export Federation (USMEF)

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

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Wine Institute of California

Olga Tuzmukhamedova

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Tel: +7 926-389-5745

E-mail: olgatuz@mail.ru

<http://www.discovercaliforniawines.com/>

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

American Chamber of Commerce in Russia

Address: 127006, Moscow, Russia, Dolgorukovskaya str., Building 7, 14th floor

Fax: 7 (495) 961-2142

Tel: 7 (495) 961-2141

Email: amchamru@amcham.ru

<http://amcham.ru/>

American Chamber of Commerce in St. Petersburg

Address: 190000, St. Petersburg, Russia, Yakubovicha str. 24, left wing, 3rd floor

Fax: 7 (812) 448-1645

Tel: 7 (812) 448-1646

Email: all@spb.amcham.ru

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

The U.S Commercial Service has offices in Moscow and St. Petersburg For questions regarding agricultural machinery, food processing, HRI equipment, and packaging equipment or materials, refrigeration equipment, and other industrial products, please contact:

U.S. Commercial Service

Bolshoy Devyatinskiy pereulok, 8

121099 Moscow, Russia

Fax: 7 (495) 728-5585

Tel: 7 (495) 728-5580

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

<http://www.buyusa.gov/russia/en/>

The U.S. Commercial Service office at the U.S. Embassy in Moscow assists American exporters by identifying potential partners through the Gold Key Matching Service. The program features:

- appointments (typically four per day) with prescreened Russian firms;

- background and contact information on each potential partner, such as: the size of the company; number of years in business;
- product or service lines; and capability to provide after-sales service;
- customized market briefing with U.S. Commercial Service staff; and,
- available market research on the relevant industry sector.

The World Bank also maintain mission in Russia.

Other Relevant Reports

Attaché reports on the Russian food and agricultural market are available on the FAS website. The search engine can be found at

<http://gain.fas.usda.gov/Lists/Advanced%20Search/AllItems.aspx>

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

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

[RSATO1205 Russian Duma Revises Wine Definitions and Other Alcohol Rules](#)

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

[Dairy and Products Annual Report 2014](#)

[Selected Poultry & Products Annual 2014](#)

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

[Exporter Guide Annual 2014](#)

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

[RSATO1312 Russian Retail Market](#)

[Fresh Deciduous Fruit Annual 2014](#)

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