

Russia's Food Processing Equipment Market

Summary

The food-processing sector is one of the leading industries in Russia's rapidly growing economy, averaging 15-20 percent growth per year for the past several years. In 2003, total industry output was valued at \$34.9 billion. Increasing consumer demand for new and better products, a population of 143 million, as well as rising incomes has greatly enhanced the development of the food industry.

Market Highlights and Best Prospects

The food processing industry in Russia started to develop rapidly as a result of the 1998 ruble devaluation. This is due to the fact that imported products became unaffordable for the majority of Russians, which necessitated domestic food producers increasing the production capacity of their factories. This in turn spurred demand for high quality food processing equipment. Local producers of food processing equipment were unable to meet the increased demand. Furthermore, the quality of domestic equipment still does not meet modern, high-tech criteria, but prices tends to be highly competitive.

Rapid growth of the Russian food industry has stimulated investments into the food sector. Russian companies took advantage of the economic crisis and rapidly began to improve the quality of their products, expand their production facilities, and renovate production equipment. Growth of food consumption in Russia has further fueled investments into the local food processing industry. By the end of March 2004, the total amount of accumulated investments reached \$57 billion, a 32.6 percent increase compared to the same period in 2003.

Global producers of food and beverages such as Coca-Cola, PepsiCo, Mars, Krafts (USA), Nestle (Sweden), Danone (France), Campina (Netherlands), Ehrmann (Germany), and Sun Interbrew (Belgium), have established local production facilities. Such international corporations have leading positions in the beverages, confectionery, yogurts, pet food, and coffee and tea sectors. While the market continues to be dominated by foreign investors, several Russian entrepreneurs have contributed significantly to the development of the sector.

Consolidation through mergers and acquisitions by both domestic and foreign business groups is accelerating in the Russian food-processing sector. The brewery industry experienced the first consolidations, which were made several years ago. Currently this trend is noticeable in the confectionery, dairy, and juice segments. In the mid 90-s, large vertically integrated holdings such as the Cherkizovsky meat-processing plant and Wimm-Bill-Dann juice and dairy producers, focused on the development of their production facilities using their own raw material resources.

A majority of the domestic players in the market are small and medium-sized companies. While large domestic companies are dominating the juice, meat processing, and vodka distillation segments, the bakery, dairy, and grocery segments of the market still have not consolidated. Major obstacles to consolidation in the industry are the country's vast geography, uneven density of the population, as well as underdeveloped distribution channels. However, the structure of the market has dramatically changed over the past

ten years. Today nearly 35-40 percent of all products are produced in Moscow and St. Petersburg. In 2003, the number of businesses in the food-processing sector totaled 22,085.

Among major new trends and processes that affect the entire food processing sector and specifically, food processing equipment, are production of new types of food products, introduction of new, high-tech machinery, technologies and techniques, and improvement in quality.

Russian food processing companies are seeking a wide variety of equipment and materials for bakery, meat, milk, oil products production, hard liquor, soft drink bottling and packaging, fruit and vegetable drying, canning, and freezing, restaurant and retail outlet equipment, fast food enterprises, and storage facilities for food products, both refrigerated and regular.

Meat Processing Sub-Sector

Market Profile

The meat-processing sub-sector is the largest food processing industry in Russia. It is currently valued at approximately \$4.7 billion. In 2003, the total food processing industry was estimated at nearly USD 34.9 billion.

Despite the fact that deterioration of equipment in the food processing industry is not as high as in other industries, the meat-processing sector needs large investments. Though production of meat products is growing, the number of new enterprises in this sector is lower than in other food processing sectors. Increasing market competition as well as the consumer's growing quality awareness are reasons why the sector must modernize.

The potential in this sector of the market is large due to the need to replace and modernize equipment. This is evidenced by the fact that approximately 84 percent of meat processing equipment has been in service for more than ten years, 14 percent for 10 to 20 years, and 2 percent for over 20 years.

Best Sales Prospects

A wide variety of food processing equipment has potentially good sales prospects in Russia. However, competition from domestic and European companies is intense.

Market experts agree that it is difficult to determine which equipment is in highest demand. They do agree that companies are at various stages of modernization, which implies that they are currently determining which equipment is needed. Thus, the potential for sales is virtually unlimited. For example, currently a number of meat processors are upgrading their technological lines, thus creating demand for such equipment. Nevertheless, the following areas represent the best prospects for U.S. equipment suppliers at present:

- Slaughter House Equipment: All equipment, but especially that for the processing of animal blood, bones, fat, and other bi-products that are usually thrown away (20-30 percent losses during preliminary meat processing).

- Butchering and make-up machinery, and shredders.
- Sausage Making Equipment: Machinery, such as grinders, cutters, mincers, injectors, heating and thermal equipment designed for processing over 10 tons of meat products per shift. U.S. companies tend to have an advantage in this area due to weak domestic competition.
- Vacuum Packaging Machinery: Vacuum packaging is progressively becoming the industry standard in Russia.
- Refrigeration Facilities: Plants with foreign investment are interested in creating modern storage facilities on site. Older central storage facilities need replacement or elimination.

As modern retail stores and food service establishments become more prevalent, the production lines and packaging for the following kinds of products are expected to be increasingly in demand.

- A variety of meat products, such as fresh meat cuts for supply to restaurants (standardized pre-cut products for the food service industry), fresh meat cuts packaged for retail sale, as well as cured, smoked, canned or cooked products, and delicatessen products.
- Semi-finished frozen meat products (i.e., hamburgers, pizzas, TV dinners).
- Russian “pelmeni” (meat ravioli) and patties: Pelmeni shops are enjoying popularity and are being established at retail stores, fast food restaurants, and bakeries.

Changes in the composition of households are influencing consumer expenditure patterns and demand for high quality prepared foods and foods prepared outside the home are experiencing rapid growth.

Import Market and Competition

The meat processing equipment market in Russia is highly competitive. European companies are aggressively marketing their equipment among viable Russian meat processing plants. European equipment dominates the import market, representing nearly 90% share. Major import markets are Germany, Netherlands, and Austria.

In order to successfully market equipment, U.S. manufacturers should be aware of how Russians tend to purchase equipment. Among key competitive factors that influence buying decisions for Russians are price, reputation, quality of equipment and machinery, availability of financial sources and after sale service. Also, it is advisable to aggressively market products and be able to provide engineering services. Further, most meat processing equipment available on the market is under warranty from three to five years.

Regarding marketing, U.S. companies should have a representative office in Russia or work through Russian distributors. Marketing U.S. equipment from the U.S. is difficult

because most Russian buyers view several pieces of equipment from different manufacturers before making their final purchasing decision. Therefore, it is important to have a company representative available to respond to questions. The company should also participate in domestic trade shows and advertise in industry magazines. Such actions will help develop name brand recognition among Russian clients.

Domestic production

Although firms appear to strongly prefer imported equipment, the market for domestically produced equipment is competitive. Russia produces limited meat processing equipment, which is known for its simplicity and reliability. By value, this equipment represents only 10-20 percent of the market. Currently, small capacity equipment is highly competitive in the Russian market and only costs 20-30 percent to comparable imports. Domestic producers of such equipment offer readily available parts and servicing. In addition, the price for local machinery is ruble-denominated and is not subject to foreign currency exchange rate fluctuations that usually alter the final price of imported machinery.

Though market experts report improvement of domestically produced meat processing machinery, Russian meat processing equipment manufacturers are not likely to make a breakthrough in production in the near future unless they can form joint ventures with foreign manufacturers. As mentioned earlier, domestic manufacturers have insignificant shares in the market. However, such factors as lower costs for domestic labor, taxes, raw materials, and energy resources also contribute to the competitiveness of domestically assembled equipment.

Among the most successful domestically produced products are vacuum mincers and small meat processing lines which produce 1.5-2.0 metric tons of meat per shift. Such equipment is successfully exported to CIS countries. Domestic manufacturers also produce equipment for small and medium-size meat shops, vacuum linking machines, smoking units, cutters, smoke generators, and ice generators. Several companies have produced their own-patented technologies. From 2002 to 2004, Russia's export of meat processing machinery totaled \$4.5 million.

Third Country Imports

In the food processing equipment sector European suppliers dominate the market. European firms consistently capture almost 90 percent of the market. Germany, Netherlands and Austria have been the consistent leaders, averaging 32.5 percent, 25 percent, and 16.5 percent, respectively. Denmark, Spain and Italy are also very active in the market. U.S. imports have been relatively small, representing only 2.7% of all imports from 2002 to 2004.

U.S. Market Position

U.S. food processing equipment was very prominent in the years following the opening of the Russian market. However, at that time competition in the market was not intense. As stated above, the U.S. share of Russia's imports of food processing machinery is insignificant. Although U.S. suppliers are currently unable to capture large market share in Russia, the U.S.'s highly sophisticated, accurate and reliable equipment is, in general, well received in the Russian market.

Market experts expect that U.S. suppliers of filling, packaging, cutting, boning, slaughtering, clipping, as well as freezing and cold storage equipment will increase their market share in next 2-3 years. Furthermore, the market situation remains favorable for American goods due to a more attractive dollar/ruble exchange rate and it appears as though more Russian companies are showing interest in American products.

A major difficulty for U.S. companies is the low level of American representation in Russia. Few companies maintain offices in Russia and American companies have little or no presence at industry trade shows. The Commercial Service in Russia encourages U.S. companies to exhibit at domestic trade shows in order to obtain better recognition among industry prospects.

Exhibiting at trade shows is an important aspect of marketing in Russia. Russians prefer to shop at the shows because they can learn from a variety of technical experts and company displays. It is important to note that different types of customer contacts are effective in Russia. For example, while some Russian companies prefer to contact U.S. manufacturers directly in hopes of obtaining lower prices by eliminating middlemen and distributors, others want to deal only with American companies which are represented in the Russian market, have offices and warehouses, and can provide designing, before and after sales services. Both methods have advantages and disadvantages. A trade show can bridge the gap and provide foreign companies the opportunity to make direct contact with potential clients.

This is evidenced by the high participation of European companies in Russian shows, which is a major source of their success in the market. European companies tend to be more successful as they are more assertive and better represented in the market than American companies. Nearly 90 percent of all foreign companies participating in Russia's trade shows are from Europe.

Market Access

Import Climate

The climate for importing meat-processing equipment to Russia is favorable. There are no quotas or limitations on such equipment. Meat processing equipment is subject to certification. However, an equipment importer is responsible for customs clearance and certification procedures.

Customs

Meat processing equipment (HS Code 8435.50.000) is subject to 5 percent customs duty and a Value added tax (VAT) of 18 percent is added to the contract value after the import duty is paid.

Representative Offices and Distributors

Distribution and business practices may vary widely, but representation in Russia is vital. A company can open an office here or market their equipment and machinery through a Russian distributor, preferably with extensive experience, good knowledge of the market,

and excellent relationships with established end-users. In this highly competitive market, most Russian customers are experienced in shopping at an open bazaar, where products are available for immediate purchase. Only advanced companies would contact an equipment supplier outside of the country.

It is also important to have Russian-speaking staff. A majority of Russian company representatives speak only Russian. Many European and Asian companies are able to communicate with potential clients in Russian.

Key Contacts

Ministry of Agriculture: <http://www.mcx.ru>

Ministry of Economic Development and Trade: <http://www.economy.gov.ru>

List of Annual Food Processing Equipment Trade Shows:

Meat Industry, February 1-4, 2006, Moscow
Processing and Packaging Equipment

VIV Russia 2006, May 24-26, 2006, Moscow

World Food 2006, September 2006, Moscow
International food, beverage, and food processing and packaging equipment.

Agroprod mash 2006, October 2006, Moscow
Machinery and Equipment for Food Processing

Golden Autumn 2005, October 2006, Moscow
Processing and packaging equipment

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