

FOOD PROCESSING INDUSTRY AND PACKAGING IN THE KHABAROVSK KRAI

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SUMMARY

Food industry is one of the rapidly developing sectors of Khabarovsk Krai economy. This sector has increased production 20 percent during the past year and today accounts for 7 percent of the Krai's overall production. Lack of sources of raw materials, high transportation costs and power and heat tariffs contribute to decreased competitive ability of the locally produced goods, and provide opportunities for importers of food stuffs from other regions of Russia and abroad. At the same time, existing demand for the domestic foodstuffs leads to the expanding market for food processing and packaging equipment. The majority of the food-processing enterprises seek for working capital in order to upgrade the quality of their products and introduce them in the neighboring markets. This report provides an analysis of the market for food processing and packaging equipment in the Khabarovsk Krai. End Summary.

GENERAL INFORMATION

Khabarovsk Krai occupying 4.6% of Russia's territory (304.5 sq. miles) has a very important strategic location on the map of the Russian Far East, and in April 2000, Khabarovsk was determined as the capital of the Far Eastern Federal District. As of January 1, 2003, the Khabarovsk Krai population was 1,470 thousand people. The Krai consists of 19 independent cities and districts, including its administrative center - Khabarovsk (600,500 people).

Khabarovsk Krai food market is comprised of locally manufactured products as well as those imported from other regions of Russia and abroad. During 2003, Khabarovsk Krai population consumed over 20 billion rubles (roughly \$ 0.7 billion) worth of foodstuffs. During the first five months of 2004, the volume of food products consumed increased 4.5 percent over the same period of 2003 and totaled 9.5 billion rubles. In 2004, the volume of meats and poultry sold increased 31 percent, milk and dairy products – 20 percent, sausages – 42 percent, confectionary – 30 percent, flour – 1 percent, vegetable oil – 60 percent.

The Share of Local Food Processing Enterprises in the Retail Trade of Food Stuffs in 2003

Product	Overall retail turnover (US\$ million)	The share of local producers of foodstuffs	
		US\$ million	Share in %
Meat and poultry	109.1		
Sausages	46.3	39.4	85
Fish products	21.2		
Canned fish	1.6		
Butter	14.53	0.4	3
Vegetable oils	15.3		
Margarine products	1.4	0.3	20

Milk	19.9	15.9	80
Cheeses	1.7		
Eggs	20.5		
Sugar	14.8		
Confectionary	46.4	5.9	12.7
Tea	1.6		
Salt	5.3		
Flour	7.7	4.3	56
Breads	40.6	40.6	100
Grain and beans	5.0		
Pasta	6.7	2.0	30
Vegetables	28.9		
Fruits, berries	33.3		
Alcoholic beverages	231.1	157.2	68

During 2003, production of the Khabarovsk Krai enterprises engaged in food and food processing industry totaled \$2 31 million (25.4 percent increase to 2002 results). During the first five months of the current year, production increased 29.9 percent and totaled \$ 119 million.

Due to its climate and territorial features, Khabarovsk Krai traditionally imports a large share of food products. The local producers are able to satisfy up to 100 percent of population's demand in breads, sausages – 85 percent, milk – 80 percent, alcoholic beverages – 68 percent, flour – 56 percent, pasta – 30 percent. Lower cost is the major reason for imports of the food products similar to those produced in the Krai from other territories. Lack of raw materials base, high transportation costs and power and heat tariffs also contribute to decreased competitive ability of the locally made goods on the Krai market.

The retail network of the Krai's food processing sector is comprised of 377 units, wholesale – 20 enterprises. The large and medium enterprises produced \$183 million worth of foodstuffs during the 2003, which is a 31 percent increase to 2002 performance.

**Consumption of the primary food products in the Khabarovsk Krai
(kilogram per person)**

	1980	1985	1990	1995	2000	2001	2002
Meat and meat products	62	66	66	50	45	49	55
Milk and dairy products	314	320	349	181	166	158	167
Eggs	289	308	283	162	196	208	209
Fish and fish products	24	27	32	16	19	21	20
Sugar	48	47	55	26	30	31	31

Vegetable oil	11.6	12.9	14.7	8.4	8.6	8.9	8.5
Potatoes	88	110	149	154	155	160	163
Vegetables	110	101	121	95	105	108	109
Fruit and berries	---	---	---	17	25	29	34
Bread and pasta, flour	131	113	115	116	120	121	119

**Khabarovsk Krai Demand in Primary Food Products as of January 01, 2004
(tons, except eggs in thousand eggs)**

Breads	6,926.6
Flour	974.6
Rice	243.4
Grain (except rice)	231.8
Bread	6,758.3
Pasta	254
Potatoes	5,429.2
Vegetables	4,773.4
Sugar	994.6
Confectionary	90.6
Beef	588
Pork	174.9
Poultry	616.2
Milk and diary	10,616.7
Fish products	840.6
Eggs	78.0
Vegetable oil	357.5
Margarines	240.4
Salt	167.9
Tea	24.2

During 2003, 54 enterprises of food processing sector were operating in the Khabarovsk Krai including 30 enterprises producing meat and diary products, 7 enterprises - alcoholic beverages, 5 breweries, four enterprises were engaged in drinking water production, 1 – alcohol, 3 – confectionery, 2 – oil and fat processing, one – tea packaging and one enterprise specializes in production of food concentrate.

The Krai government owns Khabarovsk Winery, Baby Food Combine and Lazovskiy Alcohol, and three food-processing enterprises. Five enterprises have a share of their stock in Krai ownership, including Dakgoms JSC (32.7 percent of stock is owned by Krai). Five food processing enterprises operating in the Khabarovsk Krai are in federal and three are in municipal ownership.

Khabarovsk Krai Ministry of Food Industry, Trade and Housing Services determines and controls the quality of raw materials supplied to the regional food processing sector and traces the primary sources of food stuffs. The Ministry's other responsibility is to define perspective areas for investments and development and coordinate bankruptcy procedures of unprofitable operations. Starting September 2004, the Ministry will also be responsible for the control over the genetically modified food products sold in the Krai

Increased competition on the RFE consumer market causes local enterprises to work on product quality improvement. Large enterprises usually have their own laboratories, while the other enterprises conduct physical, chemical and bacteriological analysis through specialized licensed research centers.

COMPANIES

KHABMAKARONSERVICE Joint Stock Company

For decades Khabmakaronservice has been a leading manufacturer of various pasta products in Khabarovsk Krai. In 2003 production of pasta products increased 13 percent or by 433 tons. In 1997, DAIWA Regional Venture Fund (Japan) acting on behalf of European Bank for Reconstruction and Development won the tender and acquired company's 49 percent stake held by the state for USD 500 000. The funds of USD 1,500,000 were used to finance purchase of a new Italian pasta-manufacturing line. Having new high-quality and competitively priced products the company has become a leading pasta manufacturer in the Russian Far East. Higher output has brought down per unit cost. Growing sales are supported by improvements in the area of marketing facilitated by technical consultants. Today, the company has a unique expansion opportunity, as there is a great demand for the pasta products and almost no competition in the whole Far East.

DAKGOMZ Joint Stock Company

DAKGOMZ was founded in the 60s. In 1997, State Property Committee disposed part of its equity to DAIWA Regional Venture Fund (Japan) and the European Bank for Reconstruction and Development. The Fund purchased the equity for the sum of USD 2 million used to the next purchase of a new dairy producing and soy processing equipment.

The share of DAKGOMZ in the Komsomolsk (300,000 residents) dairy market is approximately 70-80 percent and in Khabarovsk - up to 25 percent. The company delivers milk from the local farms, soybeans from Krasnorechenskoye and Vostochnoye United Producing Farms and powder milk from New Zealand. The company has a well-developed network for distribution and retail sales in both Komsomolsk and Khabarovsk. Besides DAKGOMZ is engaged in bakery, in the production of fast food products and mustard. It plans to expand the range of products by setting up the line producing cocktails containing soy products.

RAVIOLI LLC

Ravioli LLC is one of the most reputable and popular manufacturers of food products in Khabarovsk and other regions of the Russian Far East. It currently produces 31 types of semi-finished meat products and regularly introduces new industrial lines and manufacturing of new food products. The company employs patented technologies for production and know-how

technology. Ravioli currently produces 31 types of semi-finished meat products. It is a two time winner of the Russia's Top100 Products Competition. Ms. Gorokhova, Ravioli's Director General and an owner studied business management at the University of Alaska (Anchorage), and participated in business related seminars in Portland (OR). The Company has international experience.

Ravioli currently seeks US partner to provide new technologies, management knowledge/training as well as food processing equipment to expand its own production and to provide assistance to local small food-processing enterprises to develop a network of such enterprises in the Krai.

TAIGA

Taiga joint stock, is one of the leading alcohol producing enterprises accounting for nearly 30 percent of the domestic market share. Taiga delivers alcohol from Petrovsky Plant, situated in the central part of Russia. Company's strategy is to avoid the penetration of competitors allotting shares only among its employees. The company plans to develop its brewery since the RF government may any time declare the state monopoly on the production of alcoholic beverages. Taiga's management spends approximately 70 percent of dividends on construction and introduction of new products. Despite substantial demand on alcoholic drinks, currently, Khabarovsk Distillery and The Far Eastern Champagne Company have filed a petition in bankruptcy. The success of Taiga in the Far Eastern market can be explained by diversified assortment based on the production of cheap fortified liqueur made of domestic herbs.

BEST SALES PROSPECTS

Best sales prospects for the U.S. Package and Food Processing Machinery Importers to Khabarovsk Krai are as follows:

- equipment for washing and drying bottles;
- equipment for filling and packing bottles, cans, packages; attaching labels, equipment for aerating drinks;
- machines and equipment for packing and wrapping;
- equipment for milk processing;
- equipment for producing juices and other drinks;

- equipment for food processing;
- equipment for bread production, pasta and products alike;
- equipment for confectionery industry;
- equipment for producing beer;
- equipment for processing meat and poultry;
- equipment for processing fruit, nuts and vegetables and other equipment

FINANCING

Most local banks as well as branches of larger Moscow-based banks offer financing opportunities to the Krai enterprises engaged in wood processing and packaging. Majority of the food processing

enterprises is actively seeking for working capital in order to upgrade the quality of their products and introduce them in the neighboring eastern markets.

Khabarovsk branch of Vneshtorgbank (VTB) has recently organized a roundtable for the local food processing enterprises and the Krai government. All participants of the roundtable recognized the need for long-term financial resources, which will allow the sector to expand and update production. Vneshtorgbank began investing in the Khabarovsk Krai food sector three years ago. The volume of credit provided to the regional food enterprises has increased from \$200 thousand in 2001 to over \$ 11 million last year. The bank's share of financing the sector is roughly 30 percent. Further cooperation in the food sector is one of the bank's priorities in the region. VTB plans to launch specialized program for small and medium food processing enterprises, which play an important part in the sector. The Program envisions two major loan types: micro-loans and business-development loans. The micro-loans will not exceed \$ 30 thousand, while the business-development loans may amount to \$ 1 million. The average micro-loans are estimated at \$ 10-12 thousand and the development loans at \$150-200 thousand.

In 2003, Vneshtorgbank financed a purchase of water treatment equipment for Amur Pivo - the company owns and operates a medium-sized brewery (251,800 hl per year), a maltery (5,000 tons per year) and has its own network for distribution of beverages in the Russian Far East mainly in Khabarovsk Krai. Vneshtorgbank employed document financing with the attraction of the foreign bank's resources. In the nearest future, Vyazemskiy Milk Combine plans to obtain a large loan from Vneshtorgbank. The funds will be used for the production modernization and improvement of the raw materials base.

VNESHTORGBANK

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The U.S.-Russia Investment Fund makes loans to small businesses requiring financing for equipment or working capital of up to \$150,000 for first-time borrowers. Working capital loans are disbursed for up to 12 months, while loans for the purchase of property, plant and equipment are extended for terms up to 24 months. In 2003, Delt-Lease financed the project for bottling of the mineral water.

DELTA-LEASE FAR EAST

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Counterpart Enterprise Fund (CEF) program provides individual and group loans to small businesses and registered entrepreneurs including those, operating in food and food processing sector. Group loans are collateral free and range from \$100 to \$10,000. Individual loan program is targeted to larger entrepreneurs and maximum loan amount is \$15,000. Individual loans are collateralized by inventory. CEF continues a basic training program on marketing, financial analysis and business planning.

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Foreign companies have not been very active investors in to the sector. However, recently, administration of the Seoul Central Market – one of the largest in the Korean Republic plans to establish the fish-processing complex in the Khabarovsk Krai. The complex is supposed to be located near Vanino seaport and occupy 33 hectares of land. The complex will process pollack, squid, herring and other types of fish and sea products from the Sakhalin, Okhotsk and Bering seas. Its estimated production volume is 5 thousand tons of sea products per year.

CERTIFICATION

No import quotas or restrictions on food processing and packaging equipment exist in the RF. The Russian State Committee on Standards also (known as GOSSTANDART) sets all the requirements imported products must conform to. Every territory has its Regional Center on Standardization and Metrology that handles testing of equipment according to Russian standards (GOSTs). In addition, all foreign importers are to submit a certificate issued by the manufacturer that the equipment corresponds with European medical and technical standards.

A foreign company must present necessary documents proving that the equipment submits quality and sanitation tests to local acceptance standards. It also should not contain harmful substances or radiation.

STATE COMMITTEE OF SANITARY AND EPIDEMIC CONTROL OF PRODUCTS (GOSSANEPIDNADZOR)

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