Shop window on Russia

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Introduction to Russia

Russia covers an area of 17 million square kilometres. This is nearly twice the size of the United States and 71 times larger than the United Kingdom. Russia accounts for 77% of the former USSR area and 60% of its former population. Despite being the largest country in the world, Russia is one of the least populated. There are approximately 150 million people in Russia, which is just more than 2.5 times the number in the UK. From one side of the country to the other there are 11 different time zones. Despite the large land mass the majority of the population is urban. Ten million reside in the Moscow area and 6.5 million in Russia's second largest city, St. Petersburg.

The Leningrad region with St. Petersburg as its central city has a total population of approximately eight million and is 1/3 of the size of the UK. It is a western orientated city and can be considered as a 'gateway' to Russia/Europe. The current city governor, Mr Yakovlev, is very pro-reform and is seeking to increase foreign investment and trade. The area currently handles 390/, of Russia's total trade.

Structure of the bread supply industry

Prior to 1991 virtually all bread production was state owned. In the Leningrad region there were 19 large bread factories. The majority of these were within the city. There was a system of compulsory supply to retail outlets in the remote rural areas.

This system has now collapsed. Rural retailers therefore have less bread to supply and have problems with transportation costs, low profit margins and fresh bread supply. Many areas are served by a weekly delivery service. The former state owned bakeries are now privately owned, having been reorganised into joint stock companies. They still have a larger power base but many are operating at only 50% capacity. This is due to obsolete large scale equipment, raw materials supply and cash flow problems. Within the region it was estimated that there was a shortfall of 44,000 tonnes of bread for 1995.

This situation created a market force for the emergence of the privately operated mini bakery, not possible under Communism. Consequently, since 1993 approximately 150 mini-bakeries have been established. These now account for around 15% of all bread sales in the region. A recent EU study has indicated that 4,000 inhabitants are capable of supporting one Russian mini-bakery producing 1.5 tonnes bread per day. On that basis it is estimated that the market will support at least 250 additional mini-bakeries in the region. A tentative estimate has been made of a potential market in the whole of Russia for over 10,000 such mini-bakeries.
Grain and flour supply

The former USSR was a major producer of high quality breadmaking wheat. The domestic advantage and fertile soils of Ukraine, Moldova and South West Russia produced some excellent top grade flours. However, with the break-up of the USSR, Russia has lost much of that production capability.

The general decline of the agricultural infrastructure and input supply trade has seen Russia’s grain harvest swing from 107 million tonnes in 1992 to 69m tonnes in 1996. Estimates are for a total harvest of 80m tonnes in 1997. Of this, 40m tonnes will be wheat, 46% of which is of milling standard.

The net effect of all of this is that the availability of breadmaking wheat is poor. In the Leningrad region there are two major flour suppliers who are milling grain transported into the region. Due to this monopoly position and their past relationship to the ex state bakeries the availability of flour for sale to private mini-bakeries is poor. Consequently, most mini-bakeries have a large problem with continuity of supply of quality flour. There is little or no cooperative purchasing effort among mini-bakery owners.

Prices for Russian grain products in September 1997 were as follows:

f/tonne

Top-grade wheat flour 277
First-grade wheat flour 236
Hulled rye flour 217
Bread wheat 101

Sources: Informzerno

The Leningrad region has severe agronomic limitations for bread wheat production. However, with current western agronomic and flour technology it would be quite possible to increase the use of locally produced grain. In addition the development of the mini-bakery chain could be assisted with the provision of local on-farm milling facilities, should sufficient quality grain be available.

Bakery ingredients

The range and quality of Russian ingredients is poor. There is a rapidly increasing demand for improvers, emulsifiers, high quality yeast, marzipan, sugar paste, sugar craft and cake decorating.
As an example, the fermentation process used in rye bread production traditionally takes 12-16 hours. Reducing this to a four hour process has obvious implications for improvement in efficiency and is technically possible. It should be mentioned that Russians are generally proud of their bread and somewhat sceptical of western technology that may lead to a deterioration in perceived quality. However, there is also a growing sector of urban society that is demanding a fresher and more comprehensive product range than that currently available.

**Bakery equipment**

Mini-bakery equipment of Russian origin is generally of poor design. Construction in terms of hygiene, efficiency and quality is poor. Preventive maintenance and service agreements are not common. Spare parts supply infrastructure is weak. There is a high level of interest in western equipment. Turkish equipment is common but there are concerns over the operational life of these units. Power supply is a limiting factor with many rural areas having a maximum 55-60KW available.

Imported equipment, though capable of carrying significant premiums for quality, has to be competitive. There is an excellent opportunity for 'economy' models, reconditioned units and second-hand equipment. With labour costs and availability there is a good opportunity for the import of part-assembled equipment. This has the advantage of being more favourable regarding import duties.

**Skills availability**

The whole area of management and technical skills in private mini-bakeries is sadly in need of assistance. The previous Soviet state education system concentrated on large scale production. Employees were trained to a high specialist level with no concept of the whole production process.

In most industries there was a total absence of any training in business management as it relates to market economies. Concepts of profit, market research, customer care and marketing are not widely understood or practised. Bakery training institutions that currently exist are staffed by trainers from the 'old system' who perpetuate Soviet style methodologies, mainly irrelevant to today's needs. As a result of this the majority of mini-bakeries are operating at greatly reduced capacity and profitability.

Relatively simple changes in technology and processes are capable of increasing output, efficiency and product range.

Training in retail marketing and management have the potential to dramatically increase turnover. Work practice and staff management practices are poor. The development of sound business management planning and monitoring, procedures would increase the performance and survival of many new mini-bakeries.
Business profitability

The dynamic increase in the number of mini-bakeries in response to market forces is indicative of the profitability of such enterprises. Mini-bakeries are perceived as profitable but there are numerous examples of investor managers lacking the capability to manage them successfully. A recent EU funded project analysed the business performance of mini-bakeries in extreme detail. It concluded that they were inherently profitable even with unbuilt levels of debt financing for equipment purchase.

Political arena

There is an uneasy relationship between former large scale state bread factories and the newly emerging private bakeries. This gives rise to problems over raw materials supply, political lobbying and distribution. There is a young Union of Bakery Owners in St. Petersburg, representing the interests of approximately 80 mini-bakery owners.

State bread subsidies were eliminated in 1994. The Leningrad Region Committee for Agriculture is currently supporting and promoting the concept of an additional 100 mini-bakeries in the rural districts. The relationship between the St. Petersburg city administration and the regional administration is not always conducive to business development of the entire region.

UK technical assistance to the industry

ADAS, in association with Tameside College, is funded by the Foreign Office Know How Fund (KHF) to support the development of the private bakery sector. This involves the management and delivery of the 'Mini-Bakery Training Centre - St. Petersburg' project. This is also supported by commercial sponsorship gratefully received from UK bakery industry companies. The aims of the project are to.

• Establish a mini-bakery training centre This involves a training capability in both management and technical areas. Twelve trainers are undertaking intensive training at Tameside College and will subsequently deliver this to existing and new mini-bakery owners and employees. As a component of this a working demonstration bakery will be established. This has been possible due to UK commercial support This facility will serve as a 'shop window' for UK expertise and technology and should facilitate trading and investment links with the region.

• Establish a buying co-operative to support the development of mini-bakeries

the project will support the development of a buying cooperative to improve the raw. materials supply situation for mini-bakeries.

• Economic Development
Training will aim to maximise the economic performance of mini-bakeries and introduce business planning procedures to increase the success of new ventures.

• Social and political development

The training centre will help employment opportunities in rural districts and generally support the development of a market economy for bread.

• Onward investment

Through all of the project activities it is anticipated that there will be increased opportunities for UK trade and investment links.

The project commenced in May 1997. Contact details are given at the end of this paper.

Summary

The potential market opportunities in Russia cannot be ignored. The business and operating environment for trade and investment is improving dramatically. Although not an easy environment there are now many examples of UK companies operating successfully in Russia.

Opportunities in the bread industry are widespread. The observations in this paper are based on one region of Russia. It is the author's experience that similar conditions are in place throughout Russia and the former Soviet Union countries. These should not be overlooked as a means of UK business development and diversification.

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Q: Can the economy stand the cost of importing bakery ingredients. I can understand the arrangements for capital equipment, but is the cash flow there to support ingredients?

A: A short answer is yes, it can. There are major European ingredient suppliers who are trading and growing their business in St. Petersburg. I wouldn’t like to give the impression that it is an easy place – work, but with the right partnerships it is possible.
Q: Why is so much investment going into the mini bakeries and not the state bakeries which could supply so much of the bread? Of is investment going into the state bakeries as well?

A: There have been some large technical projects in St. Petersburg and Moscow which have addressed the problems of the state bakeries. What we have to remember is that the general concept of some of the funding organisations is to support the development of private enterprise and market reform. So small and medium enterprises are a key focus of their activity.

Q: You are concentrating on bread. What about other baked products such as cake? What are the possibilities there?

A: We have started with bread. and they do tend to concentrate on bread production. With a little imagination and not a lot of extra investment, they could very easily diversify into confectionery production and meat pie production. The opportunities that could grow from this are tremendous. We aim throughout the life of the project to grow into them.

Contact details

For further information on ADAS activities,
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