

Latest trends in the consumer product sector in Russia

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25 October 2018

IN ASSOCIATION WITH:



Curriculum Vitae of Dr Daniel Thorniley



Danny Thorniley is President of DT-Global Business Consulting GmbH (a LLC company), Danny's own consultancy company based in Vienna through which he works with some 330 key clients on business strategy in global and emerging markets in the CEEMEA region and Russia. The services he provides include written position papers, presentation slides and private client meetings as well as in-house presentations. He is also invited to make some 60 speeches/presentations by clients across the world on global business trends, business operations, emerging markets, corporate best practice.

Sir John Major, the former British Prime Minister has called Danny "The world's leading business expert on emerging markets"

For 23 years Danny was Senior VP at The Economist Group, Vienna on global corporate business trends.

Danny is regarded as a charismatic speaker who can present detailed business and economic analysis in an easily digestible fashion with a great deal of genuine humour. Danny is renowned for not using powerpoint presentation slides - never. Dr Thorniley has also given guest presentations at Executive MBA courses on behalf of Oxford University, the University of Chicago, IESE (Spain) and the Central European University in Budapest. The executive MBA students at Chicago rated him "best speaker" on 12 occasions out of 12 over 5 years. Danny has exceptional skill sets in global business strategy, business in emerging markets and CEEMEA and hands-operational knowledge of business operations, distribution, partnerships, investments and human resource issues.

He has worked on a personal basis with 330 companies operating in emerging markets for 27 years and has personal contacts with most senior western MNCs operating in the CEEMEA region and beyond. He makes frequent presentations at CEO and Board level (over 100). He has personal friendships with leading executives in Coca Cola, Procter & Gamble, Ernst & Young, Raiffeisen, Robert Bosch and many, many others.

He holds and has held a number of non-executive and advisory board memberships with major European and US corporations including the Global Advisory Board of the US company Aecom.

Dr Thorniley was educated at Oxford University. He holds a Bachelor of Arts degree, a diploma and a doctorate degree in Soviet political economy.

He has published three books, including one on Russia with Macmillan (UK/USA) and two with Profile books on Doing Business in Global Emerging Markets.

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Latest trends in the consumer product sector in Russia: Influences on your 2019 Budget

What goes on with the Russian consumer affects nearly all corporate executives operating in the country and not just those in consumer product companies. Business ends up eventually with the end consumer for 80-90% of all companies and hence why this update is important for nearly all executives in the Russia-CIS Business Group.

Our summer 2018 Report on Consumer Product Trends in Russia remains almost entirely valid. Our most recent October summary of business and economics for the 2019 Corporate Budget also provides the corporate business numbers:

If you missed either of these reports I urge you to read them! It's worth the effort. 😊

Quick sales numbers for CP companies in Russia in 2018 and budget forecast for 2019

First off, consumer confidence deteriorated in Q3 of 2018 from -8 to -14 and this was the first fall since January 2016 (more below).

Sales growth in roubles, 2018 and 2019												
	All Companies			Consumer Prod.			Pharma/Health			B2B/Industrial		
	2018	2019	Δ	2018	2019	Δ	2018	2019	Δ	2018	2019	Δ
Growth of 20%+	10	3	-8	7	0	-7	0	0	0	15	5	-10
Growth of 10-20%	21	21	0	26	25	-1	27	27	0	17	16	0
Growth of 5-10%	27	40	13	30	39	8	27	40	13	24	41	17
Growth of 1-5%	15	21	6	12	27	16	33	27	-7	12	15	3
Flat-zero	7	11	4	7	7	0	7	0	-7	8	16	9
Decline of 1-5%	6	2	-5	9	2	-7	0	7	7	6	0	-6
Decline of 5-10%	8	3	-6	7	0	-7	0	0	0	11	5	-6
Decline of 10-20%	2	1	-2	0	0	0	7	0	-7	3	2	-1
Decline of 20%+	3	0	-3	2	0	-2	0	0	0	5	0	-5

Source: DT-Global Business Consulting, Russia-CIS Business Group Survey. September 2018. Number of responses, in %.

Consumer product companies have had a bumpy period with 37% reporting flat or negative rouble sales in 2017. While the beginning of 2018 showed some improvement for most in the industry with only 7% reporting flat or negative sales growth, the numbers have declined over the year and now 26% report flat or negative growth. For the 2019 budget, most companies are optimistic and cluster around the single-digit growth region (66%) and some expect double-digit growth (25%).

So a tougher 2017 for many; better plans for 2018 which did not come to fruition for everyone; and hopeful better plans for 2019.

Some of the most recent economic numbers affecting consumer products in Russia

But some executives are a bit doubtful about trends because of all the business features below.

The Russian Statistical Agency Rosstat published some consumer sector numbers in recent days and we share key highlights here:

- Retail sales in September grew by just 2.3% compared with 2.8% in August (but the higher figure could have been a remnant of the World Cup)
- Most of the retail sales slowdown was due to falling food purchases rather than non-food which rose by 4.1% in September.
- Consumers with smaller income may be cutting back on food or more likely buying cheaper products
- So retail sales were ok but not great considering that unemployment is down to a low of 4.5% in September
- And when real wages after inflation are still surging at 7.2%

- **BUT public sector wages are rising much stronger by +19% in September which implies that salaries in the private sector are tighter. So NOT ALL employees are necessarily on a pay boom.**
- And the “devil is in the detail” regarding disposable incomes. This is an indicator we do not usually like to employ as it has too many variables including FX sales by citizens so a “wobbly” indicator.
- However, we note that “real disposable incomes” are composed of 66% salaries but the remainder includes proceeds from entrepreneurial activity, social payments and rents etc. In recent years pensions have been frozen and only indexed a bit at the start of 2018 while income from entrepreneurial activity” has slumped in the last 3 years.
- **Conclusion: some public sector salaries are booming, private ones less so and income from non-salary sources has weakened through 2015-2018.**
- **This is another explanation why underlying spending may be weaker than “it should be”**
- Also retail loans growth has boomed by 22% in September. BUT as we have pointed out, consumers use credits for cars and mortgages and then curtail spending on other consumer products
- But in recent months the consumer has been hit by a weaker rouble, higher fuel prices, higher interest rates and creeping inflation and deep concern about the pensions outlook
- Public approval ratings for the government and President have slumped due to the pension announcements and as we noted above, consumer confidence deteriorated in Q3 this year from -8 to -14 which was the first fall in this indicator since January 2016.
- We will see if tighter fiscal policy is moderated a bit in 2019-2020 or not much.
- And consumer confidence deteriorated
- This would suggest that the savings ratio has started to rise, although we do expect a flurry of consumer product sales as consumers “buy in ahead” of the VAT increase in January 2019.

The Russian consumer – key features

1. The Russian consumer has changed radically in the last 2-3 years making business tougher for FMCGs.
2. The Russian consumer is less resilient and more normalised (western).
3. The Russian consumer has been getting more “tired” since about 2016-17. The consumer went through 2013-16 quite well and proved resilient for western FMCGs but that cycle has run out of steam along with the ability to raise prices. The consumer is more demanding and wants good quality at a cheap price.
4. The Russian consumer is getting less loyal??
5. The relatively stronger rouble means that more tourism abroad takes place and Russians spend some of their disposable income outside Russia.
6. When consumers have spent money on their holidays or 2-3 short foreign holidays, they are and they feel less rich.
7. Promos and discounts....consumers have gotten used to this and will find it hard to change habits.
8. Government spending is not supportive of consumer spending. Government fiscal policy has been austere in 2014-18 and interest rates tight. Proportionately less spending has gone on education and health. We will see if there is more social spending to come.
9. This means that consumers need to save “for a rainy day” and think of covering their own health and educational needs. They spend on health and not detergents or chocolates.
10. Consumer credit is now rising by more than 20% in autumn 2018. BUT most of this goes on mortgages and cars. So, once again the consumer has less disposable income to spend on other consumer items or only wants to buy cheaply.
11. E-commerce could be a help or, as we see in other slides, a disruptive threat.

12. The Russian consumer in some age categories is getting increasingly worried about their pension outlook and rightly so. This dampens spending patterns.
13. Recent price rises (since autumn 2016) are much tougher to get through thanks to the stronger rouble and lower inflation.

Some of the key business issues facing senior managers in consumer product companies

- E-commerce has started to disrupt business.
- As we note, if more sales are channelled through web platforms and logistics companies, why do you need so many traditional distributors?
- Age profiles are defining the business more than income ones.
- What will be the impact on traditional brands as younger people dominate trends and perceptions if not yet the buying power.
- What's the future for traditional brands in Russia and globally.
- How will you structure your e-commerce business: just a part of the regular business with people double-jobbing or is bigger change needed: do you need a separate company and ethos? Maybe yes, maybe no.
- E-commerce has started to disrupt the HR market: where do you find good e-commerce staff who can drive your business.
- Why will young dynamic entrepreneurs in e-commerce want to work in "My boring company" to quote the MD of a large FMCG company.
- Can you launch a new product quickly in this changing environment or is your Russia business ham-strung by international corporate bureaucracy?
- "If I don't raise prices, then my profitability is hurt and my HQ complains. If I do raise prices now, then my categories and market share are hurt as well"
- Another problem is that consumers are "buying into the concept" of upward innovation much less than in recent years, so upward innovation is harder
- CP companies could always raise prices aggressively in 2015-16 and most of 2017 but this option has mostly evaporated
- "I launch sub-premium brands to capture those who can't afford the big brands at full price"
- "The top and bottom of the market are good for me: but the mid-price and mid-brand sector are hell for us and everyone else. How do we fix that?"

I hope this commentary helps you in your business planning and I look forward to greeting you at the remaining autumn executive meetings.



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Eric Poulet,
Supply Chain Director, Leroy Merlin

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Leroy Merlin's sought to build an omni-channel national distribution center as well as an e-commerce fulfillment center. With our unique expertise in e-commerce and our proprietary Radius InSite Digital 5D Design Modeling & Construction Analytics Platform, we delivered the design Leroy Merlin wanted and the building they needed, on-time and on-budget.

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