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RESEARCH

FOOD RETAIL AND CONSUMER MARKET OF RUSSIA

Trends 2017
Growth prospects in 2017-2019
DEMO VERSION

INFOLine
информационное агентство information agency

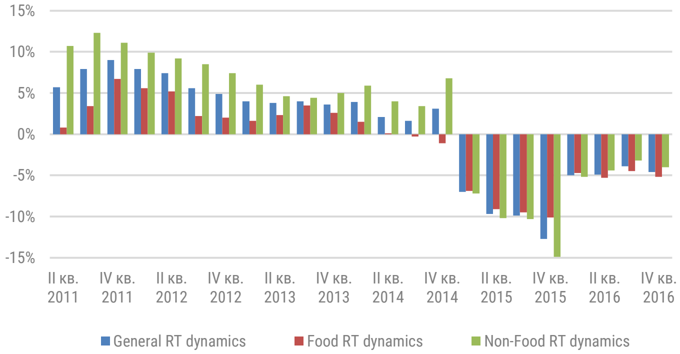
- KEY RETAIL HIGHLIGHTS
- KEY FMCG RETAIL EVENTS
- RATINGS OF FMCG RETAILERS
- OUTLOOK FOR FMCG RETAIL GROWTH
- MARKET SURVEY OF FMCG SUPPLIERS

TABLE OF CONTENTS

1.1. RETAIL TURNOVER

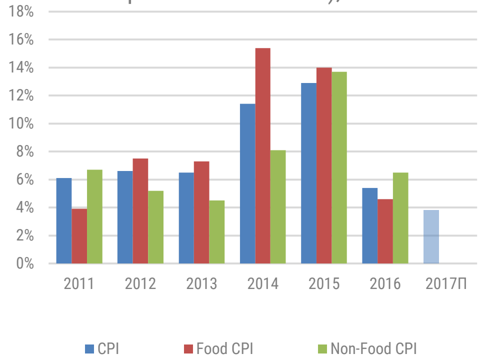
- In 2016 the retail turnover (RT) decreased by **4.6%** expressed in physical terms to **28317.3 bn. RUB**. However, in monetary terms RT increased by **2.9%.** In 2017 the Ministry of Economic Development of the Russian Federation anticipates transition in the RT dynamics expressed in physical terms towards the area of positive values while in 2018 - increase of the growth rate almost up to the growth rate level fixed in 2014.
- In the situation of decline in the population real income by **5.9%** over 2016, despite rationalization of the consumer behavior, in 2016 the share of expenses for goods and services purchase in the household budgets increased by **0.8 p.p.** and **0.4 p.p.** At the same time, the revenues intended for savings, decreased by **3 p.p.**
- Against the background of the high basis in 2015, the decrease of the consumer activity and the ruble strengthening in the H2 year, in January-December 2016 the annualized inflation slowed down to **7.1%** against **15.5%** in January-December 2015. Meanwhile, in January-December 2016 the annualized Food CPI demonstrated the lowest indicator over the last 10 years – **6%** (the lower indicator was registered only in 2013 being equal to **3.9%**). Under the conditions of the maintained moderately stringent monetary policy the Ministry of Economic Development of the Russian Federation forecasts the average CPI for 2017 as **4%** by the end of the year (December 2017 against December 2016) – **3.8%.**

Retail turnover, in % to the corresponding period of the previous year



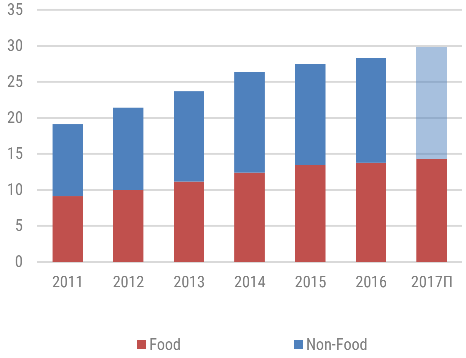
Source: FSGS, INFOLine assessments

CPI dynamics and forecast (December against previous December), %



Source: FSGS, EMR

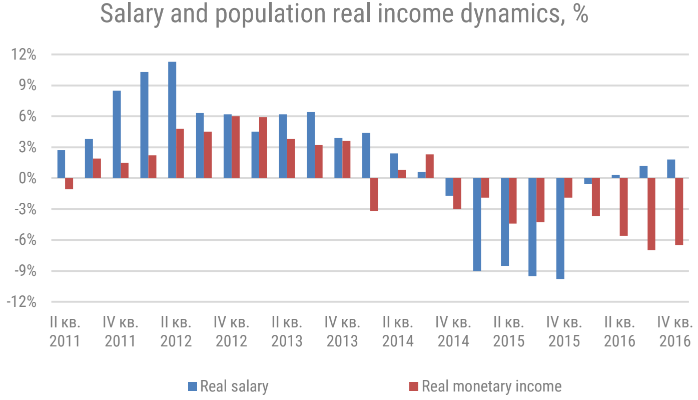
RT dynamics per segments, trillion rubles



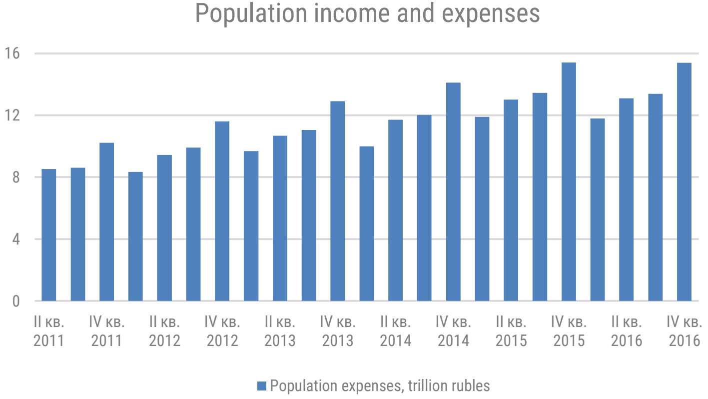
Source: FSGS, EMR, INFOLine assessments

1.6. POPULATION INCOME AND EXPENSES DYNAMICS

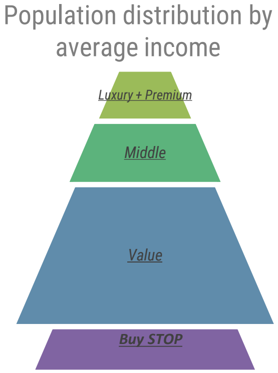
- By the end of 2016, the population income has been reduced for 26 months and, despite the decline slowdown to **-2.7%** in September 2016, by December 2016 the decline again accelerated and was equal to **-6.8%.**
- At year-end 2016, the reduction of the population real income accelerated by **5.9%** (in 2015 the reduction was equal to **3.2%)** while the real income increased by **0.7%** (after the **9%** reduction in 2015). The one-off payment to the retirees equal to 5,000 rubles in the beginning of 2017 resulted in a sharp income increase, thus, the Ministry of Economic Development expects the population real income growth at the year-end for the first time since 2013 (by **3.3%).**
- As of the results of Q4 2016 the population confidence index increased by **1 p.p. (-18%)** against Q3 2016, the enabling index for large purchase remained the same **(-33%)** while the savings enabling index reduced by **1 p.p.** (**-42%**). **84%** of the FSSS surveyed consumers pointed out that now is not the best time to spend money (against **73%** as of the Q4 results, 2015) while **75%** of the consumers in Q4, 2016 reduced their expenses to the level of Q4 2015 (with the indicator of **73%** in Q3 2016).



Source: FSGS



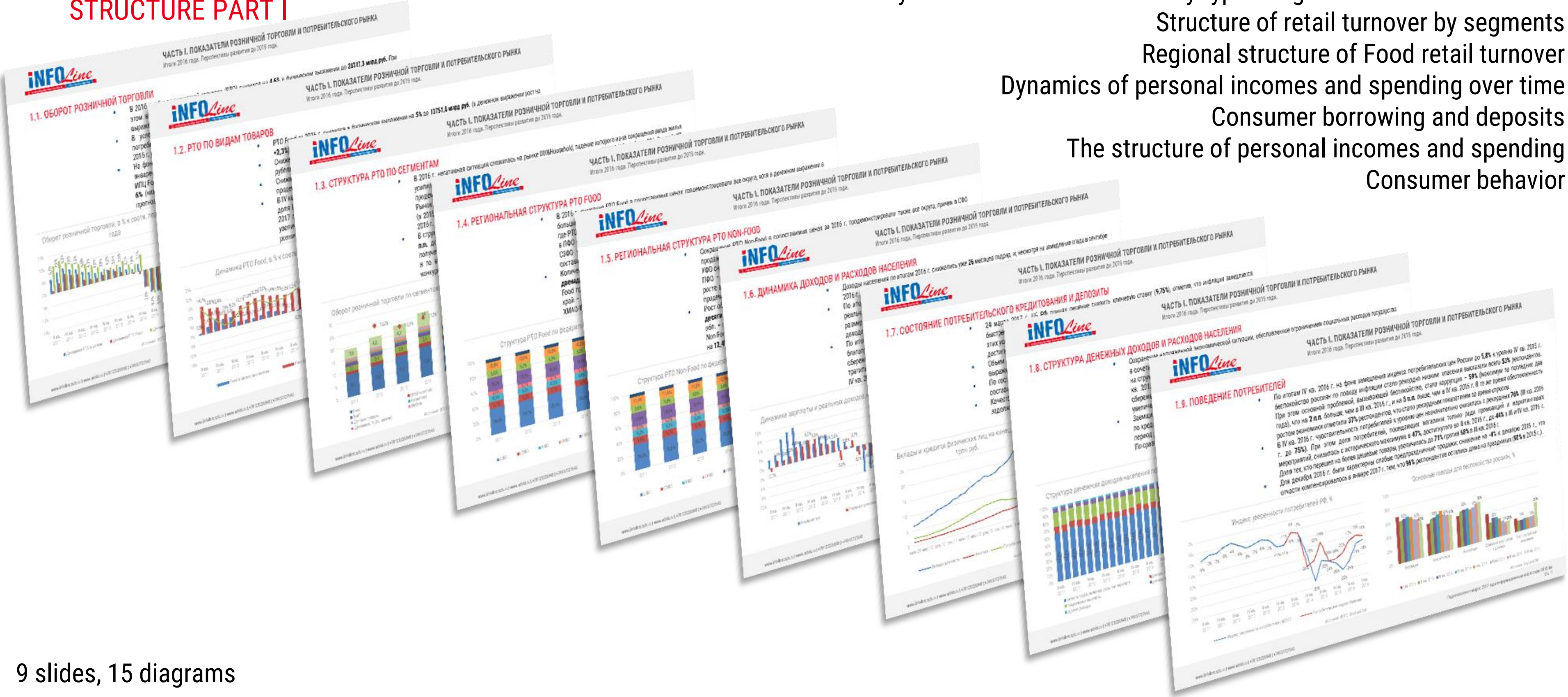
Source: FSGS



Source: FSGS, INFOLine

STRUCTURE PART I

Dynamics of Retail turnover by types of goods Food and Non-Food
Structure of retail turnover by segments
Regional structure of Food retail turnover
Dynamics of personal incomes and spending over time
Consumer borrowing and deposits
The structure of personal incomes and spending
Consumer behavior



9 slides, 15 diagrams

2.1.1. GOVERNMENTAL CONTROL OF RETAIL TRADE

- **On January 1, 2017**, the interim period (from July 15 until December 31, 2016) expired, and the amendments to the Law on Commerce became fully effective. On July 3, 2016, the President signed the **Federal Law N 273-FZ of 3/7/2016** (text of the document) introducing the concept of "merchandising services" and stipulating that the aggregate amount payable by suppliers of groceries to trade enterprises shall not exceed 5% of purchased goods. The law also streamlines the acceptance of goods and reduces the terms of payment for supplied groceries. **On November 18, 2016, the Russian Federal Antimonopoly Service (FAS) published the second package of explanatory notes (text of the document).** The first package was released on September 5, 2016 (text of the document). And on June 9, 2017, **the FAS published the third package of explanatory notes** on pricing and discounts (text of the document).

- **In Q1 2017, the FAS of Russia audited contracts concluded** between retail chains and food suppliers after July 15, 2016, in order to validate them against the new provisions of the Law on Commerce. As of March 10, 2017, the regional offices of the Russian FAS carried out **701 audits** and reviewed **11,266 contracts** revealing **1,261 violations** (about 11% of all audited contracts). As a result of the audit, the most common violations were the non-compliance of documents with the **new provisions of the law – 439 contracts** (**34%** of all identified discrepancies) and **the excess of the allowed 5% fee – 282 contracts (22%**). Also, the FAS detected facts that retail chains, having formally brought their contracts into compliance with the updated law, **entered into service agreements with third-party controlled entities,** which ultimately led to the suppliers' obligation to pay more than 5% fee. In most cases, violations were revealed in the business of regional and municipal retail chains. And on June 5, 2017, the FAS launched a hotline about violations of the Law on Commerce.

- **In 2017, the Russian Ministry of Economic Development plans to assess the actual impact of the Law on Commerce.** The audit may result in "decisions to amend the legal act or to revoke it, as well as make other decisions based on the findings".

STRUCTURE PART II

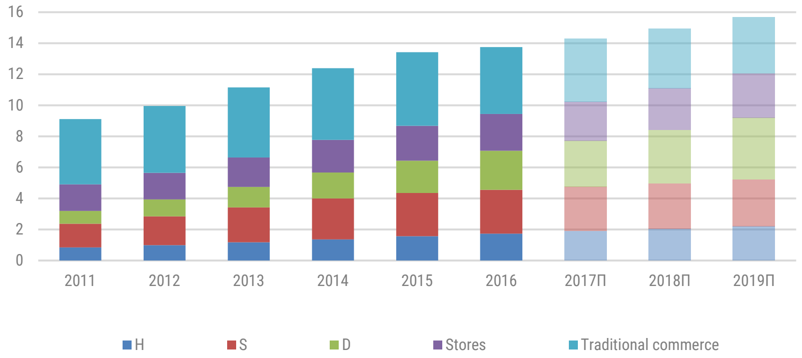
Events and actions of international companies
Governmental control of retail trade
Governmental control of FMCG retail
Milestones and business of global companies
FMCG quality control

8 slides

3.1. TURNOVER STRUCTURE OF FOOD RETAIL MARKET

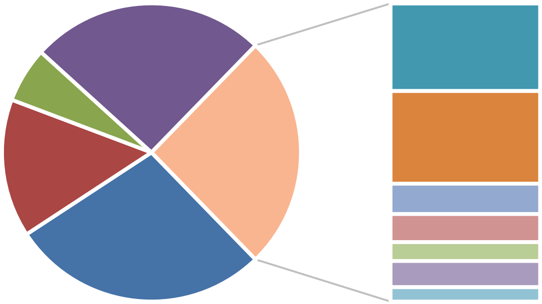
- In 2016, D and H formats growing by **22%** and **10%,** respectively, demonstrated the most fast-paced growth among retail formats due to the investment spree of federal retailers.
- Impacted by low consumer incomes, the S format suffers most because customers switch to more cost-saving formats: the growth of Food retail turnover in S format amounted to slightly less than **1.5%** in 2016. Thus, a number of companies postponed or changed their plans for S format growth. So, Azbuka Vkusa (www.av.ru) that previously planned brisk growth of its AV Market format, focuses on the small format AV Daily due to its better performance.
- In 2017-2019, there is a persisting trend towards less traditional retail outlets and a surge in the number of small modern formats (D and C).

Food retail turnover by sales channels over time, tln RUB.



Source: INFOLine asessements

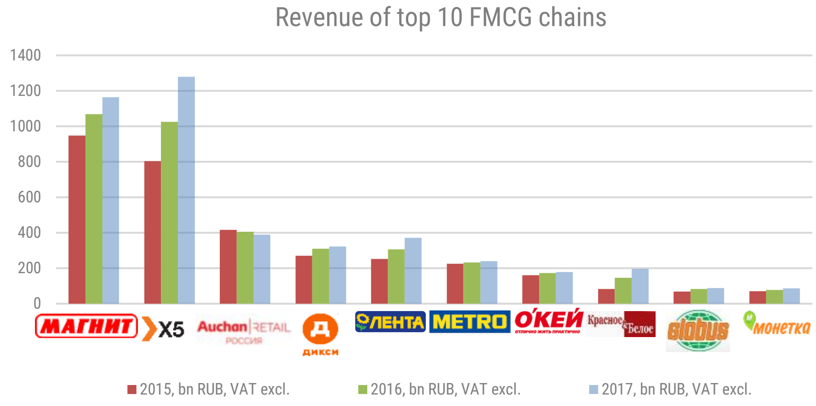
Russian food retail market structure in 2016, %



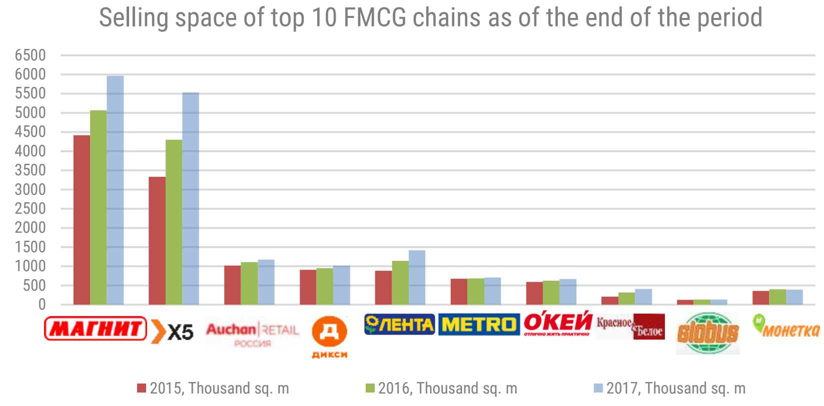
Source: INFOLine asessements

3.5. RATING OF TOP 10 FMCG CHAINS

- In 2016, X5 Retail Group (www.x5.ru) kept its leadership in the pace of new openings and selling space adding **2,167** stores and **969.6 Thousand sq. m.** Until 2020, X5 plans to maintain growth rates and open at least **2,000** stores annually, mainly Pyaterochka D stores.
- Magnit chain (www.magnit-info.ru) reduced its growth pace in 2016 year-on-year adding **1,961** stores and **654 Thousand sq. m**. In 2017, Magnit plans to amplify its investing activity primarily through the growth of D stores – **1,600-1,700** new openings (927 in 2016), renovation of **2,000 D** stores with their transformation into Magnit C format and drogerie stores – **1,000** stores (**986** in 2016). Still, the opening rates of H and S stores in 2017 will be lower than in 2016: **15** H (**18** in 2016), **25 S** stores of Magnit family format (39 in 2016). In 2017, Magnit's capex will exceed **RUB100bn**, of which **RUB20bn** will be spent on store restyling, and **RUB5-7bn** will be directed either to the acquisition of local chains, or to the organic growth of the chain.



INFOLine assessments

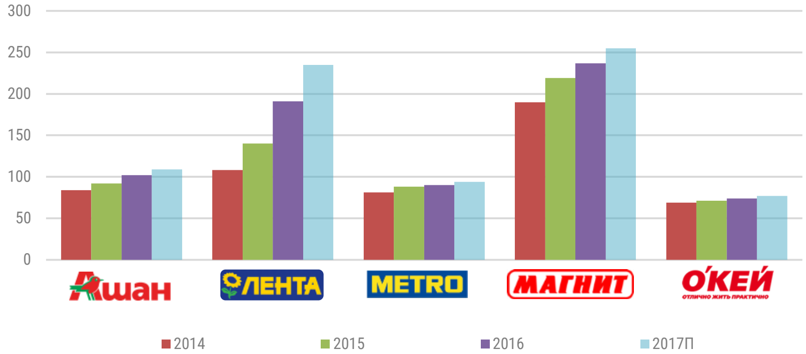


INFOLine assessments

3.8. RATING OF FMCG RETAIL CHAINS BY FORMATS: H

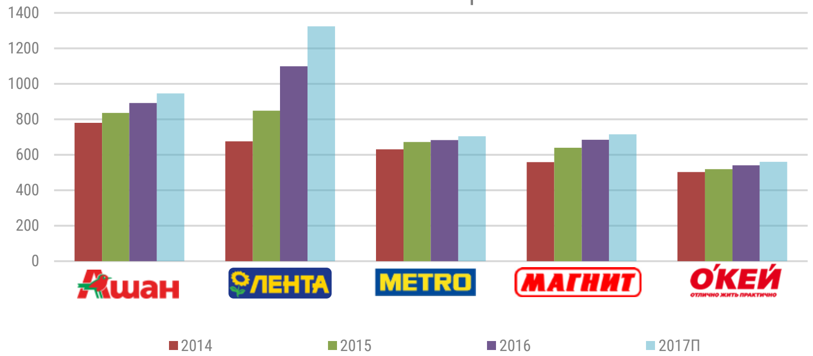
- In 2016, the front-runner in opening H stores was Lenta (www.lenta.com) that opened **51** H stores and expanded its total selling space by **251 Thousand sq. m**. In Q4 2016, Lenta made a number of changes in the selling space of its existing H stores, as a result of which the space was reduced by **311 sq. m.** The Far Eastern chain Samberi (www.samberi.com) opened **5** H stores throughout 2016 **(2** of which were opened in Q4) with about **21.6 Thousand sq. m** total space. Thus, the absolute leader in the Far Eastern Federal District increased its investing activity after the opening of only one H in 2014 and no openings in 2015. In 2017, it plans to open at least **2-3 new H stores.**
- For the first time after 2009, Matrix chain (www.matrix-m.ru) resumed the development of the format by opening an H store in Moscow with **2.5 Thousand sq. m** selling space in Q4 2016, and the Tabris chain (www.tabris.ru) opened the first H in Krasnodar with **2.5 Thousand sq. m** selling space.

Number of stores of top 5 FMCG chains in H format as of the end of the period



Source: INFOLine, «FMCG H markets in Russia. The outline of 2016. Forecasts till 2019 »

Selling space of top 5 FMCG chains in H format as of the end of the period, Thousand sq. m



Source: INFOLine, ««FMCG H markets in Russia. The outline of 2016. Forecasts till 2019 »»

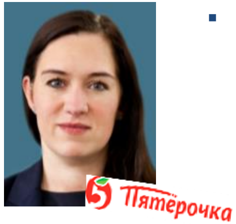
3.12. RESIGNATIONS AND APPOINTMENTS

- On May 10, 2016, Andrey Elinson, one of the directors of ABH Holdings S. A., Alfa-Bank (Russia), a member of the Supervisory Board of **X5 Retail Group** and a member of the Board of AlfaStrakhovanie Group, was appointed for the Supervisory Board of X5 Retail Group (www.x5.ru).

- On August 17, 2016, **Dmitry Himmelberg**, ex-Deputy CEO for Strategic Development of Transmashholding Group, was appointed CFO of **X5 Retail Group (www.x5.ru).**

- On August 22, 2016, **Maxim Gatsuts**, ex-COO of Metro Cash&Carry Russia (www.x5.ru) was appointed CEO of **Karusel** chain (www.karusel.ru) belonging to **X5 Retail Group (www.x5.ru).**

- On September 19, 2016, **Pavel Lokshin,** ex-CEO of the Finnish chain K-Rauta (www.k-rauta.ru), was appointed CEO of **Perekrestok-Express** chain belonging to **X5 Retail Group (www.x5.ru).**



- On October 1, 2016, **Yulia Tyuleneva** was appointed CEO of the Siberian **Division of Pyaterochka (www.5ka.ru).** Her main function will be the expansion of Pyaterochka in the Siberian Federal District: the opening of stores in Novosibirsk, Kemerovo, Novokuznetsk and Omsk. Previously, Yulia led the cluster in the Central Division.

- On December 1, 2016, **Vitaly Valkov** was appointed CCO of **X5 Retail Group (www.x5.ru)**, replacing **Vladimir Sorokin,** who also managed Perekrestok chain. Vitaly Valkov is also CCO of Perekrestok chain.

- In March 2017, **Ekaterina Lobacheva** was appointed the Director of Legal Support of **X5 Retail Group (www.x5.ru)**. Prior to joining X5, Ekaterina held executive positions at EvrazHolding LLC, worked for such companies as MDM Bank OJSC and the Investment Building Holding.

STRUCTURE PART III

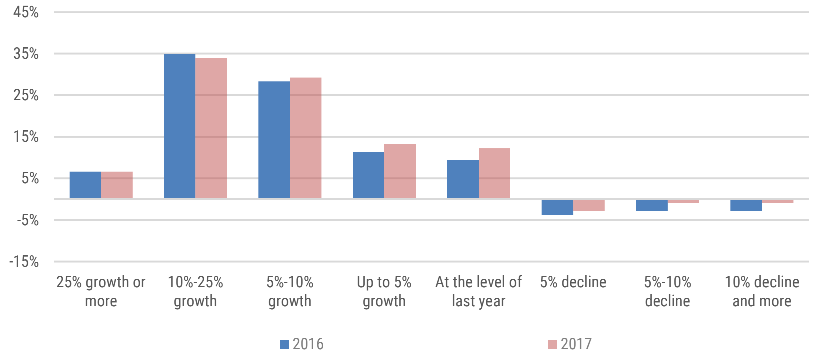
Turnover and structure of food retail market
Investing activities
Rating of retail chains
Rating of FMCG retail chains by formats
Dynamics of the operational indicators
M & A deals, resignations and appointments
Entering the RC of FMCG

23 slides, 26 diagrams

4.1. SALES OF TOP FMCG SUPPLIERS OVER TIME

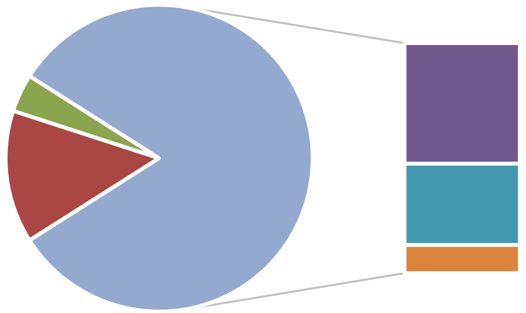
- The retail turnover in the food segment lost **4.6%** in real terms in follow-up of 2016, but (taking into account price spikes) increased by **2.3%** in terms of value.
- Following the results of 2016, the reduction in real personal incomes accelerated to **5.9%** (decreased by **3.2%** in 2015), and real wages grew by **0.7%** (after **9%** decrease in 2015).
- The vast majority of the largest food suppliers demonstrated sales increase in rubles – **80%** of respondents. More than **40%** respondents cite 10%+ sales growth.
- INFOLine's outlook proved true: the sales growth of the largest suppliers amidst the market slump as a whole was driven by the inflation and market consolidation (shakeout of small players and import substitution).
- Most respondents express optimistic outlooks for sales in 2017 – **80%** of respondents expect sales to increase in 2016, only **4%** anticipate some decline.

Sales of the largest FMCG suppliers in 2016 (RUB) and the outlook for 2017.



Source: INFOLine asessements

Plans connected with sales changes by FMCG suppliers in 2017, %



Source: INFOLine asessements

STRUCTURE PART IV

Dynamics of sales of top FMCG suppliers
The share of sales of top suppliers in FMCG chains
Company growth and governmental control
Cooperation of top suppliers with FMCG chains

4 slides, 8 diagrams

5.1.1. X5 RETAIL GROUP

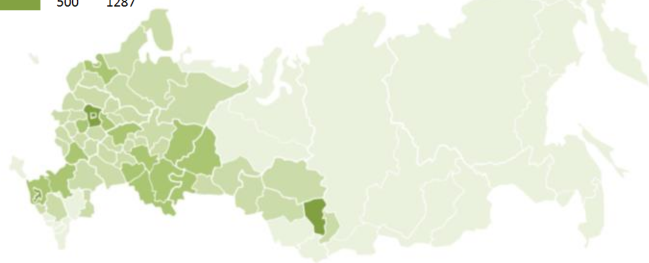
- **In 2018**, X5 Retail Group **plans to complete its renovation** of existing stores of all formats (D, S and H).
- **As of April 1, 2017, the share of stores** branded by the new concept reached **96% of all Pyaterochkas and 56% of all Perekrestoks.**
- **In 2017-2019**, X5 Retail Group seeks to put into operation about **36 DCs** and more than **500 Thousand sq. m** of new DCs for Pyaterochka, Perekrestok and Karusel chains.
- **In April 2017, X5 Retail Group signed the Cooperation Agreements with Centrosoyuz of the Russian Federation for 5-year term.** The potential of the project named **COOP-Pyaterochka** is estimated at **1,000 stores** during the first three years. **Also, it is planned to open up to 5,000 brand-name sections in the shop-in-shop** format in **Pyaterochka** stores selling farm products and goods of consumer cooperatives **up to 2021.**

X5 Retail Group's reach:

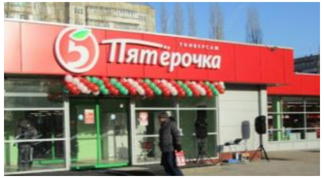
Кол-во магазинов

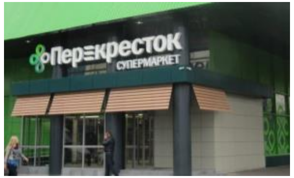
0	0
1	149
150	499
500	1287

Chain stores: Volga, North-Western, North Caucasian, Siberian, Ural, Central, Southern Districts



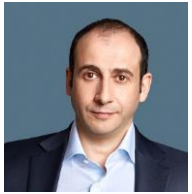
Formats





Top management

Stephan Ducharme, Chairman of the Supervisory Board

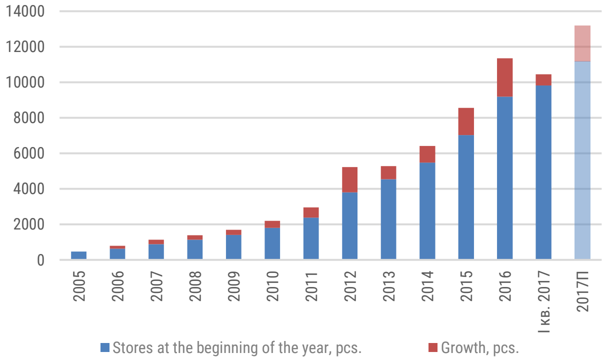


Igor Shekhterman, CEO

5.1.1. X5 RETAIL GROUP

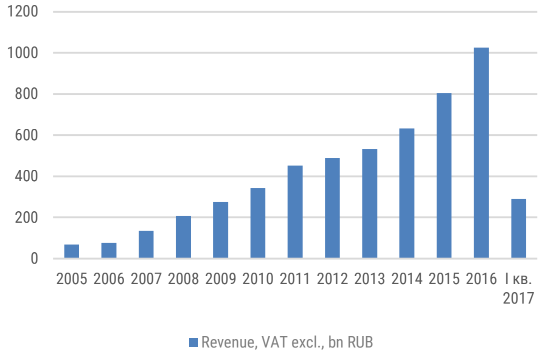
- In Q1 2017, the net growth of X5 Retail Group was **630 stores: 639 soft Pyaterochka D stores, 5 Perekrestok S stores. 13 Perekrestok Express stores and 1 Karusel H were closed**. In 2017, X5 Retail Group seeks to open more than **2,000** stores mainly through organic growth, but taking into account tactical M&A in the regions.
- According to the results of Q1 2017, the retail revenue of X5 Retail Group reached RUB291.484 bn (+26.4%). The LFL sales of the company reached 7.3%.
- X5 Retail Group intends to **double its business by 2020** focusing on organic growth: X5 Retail Group plans to get a **15% share of the Russian FMCG market** in **3-4 years**.
- Until 2020, X5 Retail Group plans to maintain capex at around **RUB80bn** annually and to open at least **2,000** stores per year. About **70**% of capex will be spent on **store openings**, 30% – on **supply and IT development**.

Dynamics of X5 Retail Group's stores



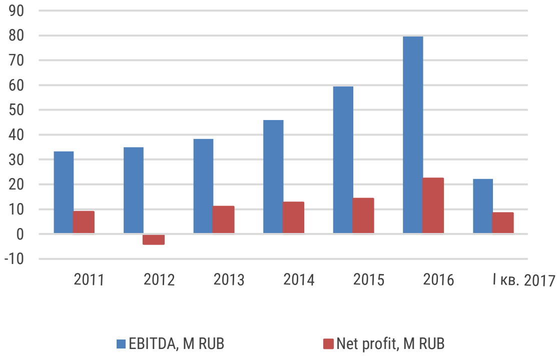
Source: corporate data, INFOLine

X5 Retail Group's revenue trend



Source: corporate data

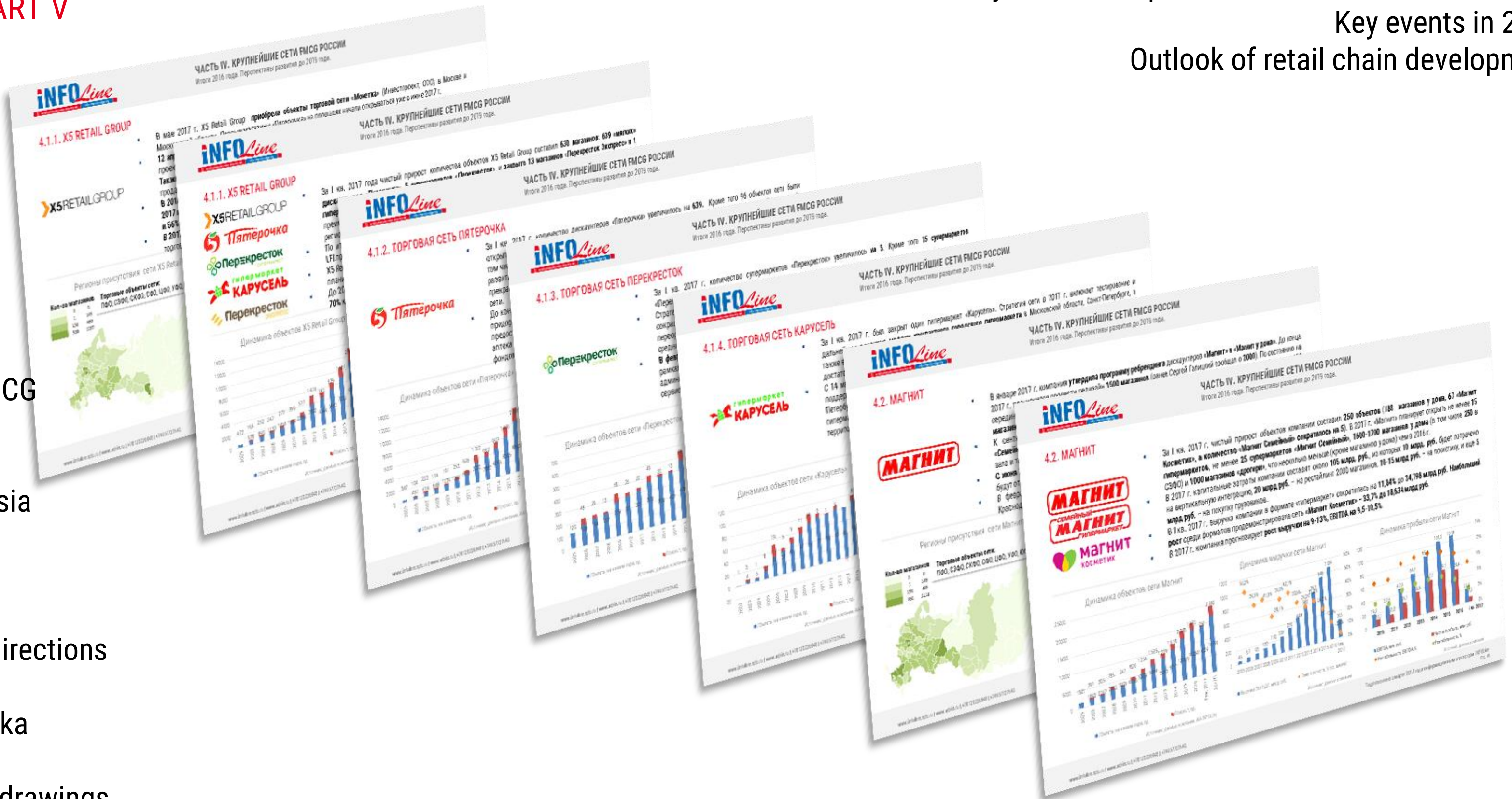
X5 Retail Group's profit trend



Source: corporate data

STRUCTURE PART V

Dynamics of operational and financial indicators
Key events in 2017
Outlook of retail chain development



TOP-7 companies FMCG

- X5 Retail Group
- Magnit
- Auchan Retail Russia
- DIXY
- Lenta
- OKEY

2 leaders of special directions

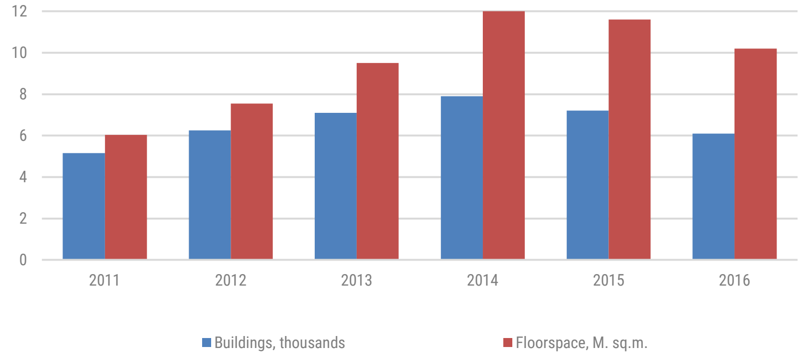
- Red & White
- VkusVill and Izbenka

21 slide, 36 charts, 9 drawings

6.1. HIGHLIGHTS OF COMMERCIAL PROPERTY MARKETS

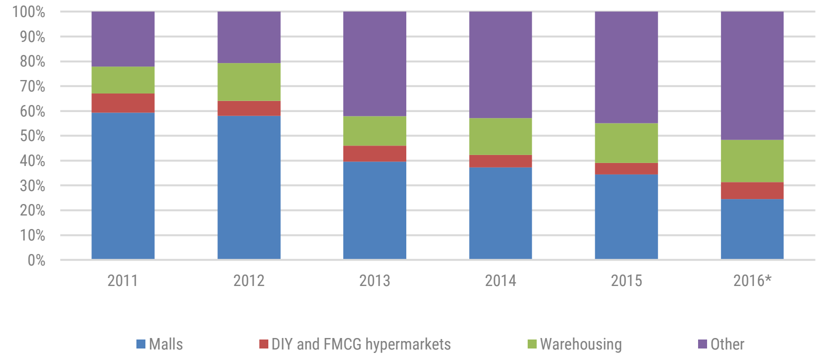
- In 2016, **12%** less commercial buildings were commissioned compared to 2015: only **10.2 million sq.m.;** categories affected the most were malls (**38%** less space commissioned) and warehouses (**7%** less).
- FMCG hypermarkets make up for **5%** of the total commercial property commissioned; in 2016. **114 such hypermarkets** were opened with their total floorspace equaling **895 thousand sq.m.;** 59 of those occupy stand-alone building of a total area of **495 thousand sq.m.**, which is **14%** less than in 2015. The largest hypermarkets then commissioned are: Globus (29 thousand sq.m., Odintsovo); O'KEY (19 thousand sq.m., St. Petersburg), and Lenta (Yekaterinburg, 14 thousand sq.m.).
- As of DIY, **33** new hypermarkets were opened, **17** of which are Leroy Merlin; however, **34** existing supermarkets were closed, including **ten** Metrika and **seven** Superstroi hypermarkets. **22** of the DIY hypermarkets commissioned occupy stand-alone buildings with a total floorspace of **210 thousand sq.m.,** which is **23%** more than in 2015.

Commissioning of commercial buildings in Russia



Source: INFOLine assessments,, FSGS, UISFS

Structure of commercial buildings and malls commission in Russia, %



Source: INFOLine, Research "Market of Russian shopping malls" data, FSGS, UISFS

STRUCTURE PART VI

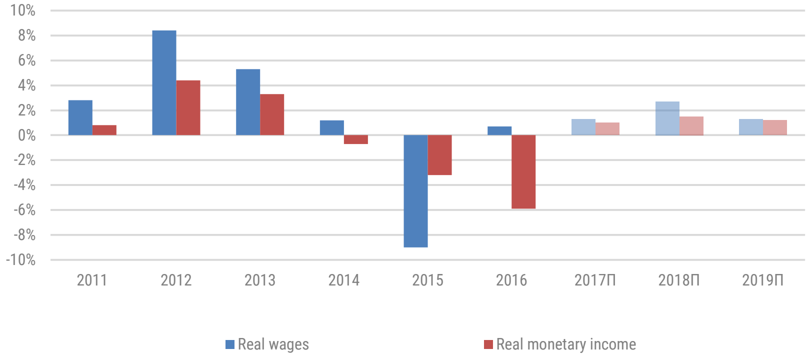
Key highlights of the commercial real estate market
Largest commissioned shopping malls
Rating of mall owners INFOLine Developer Russia TOP
Key events in the market of shopping malls
Projects of shopping malls at early construction stages

12 slides, 5 diagrams

7.3. OUTLOOK FOR PERSONAL INCOME AND SPENDING

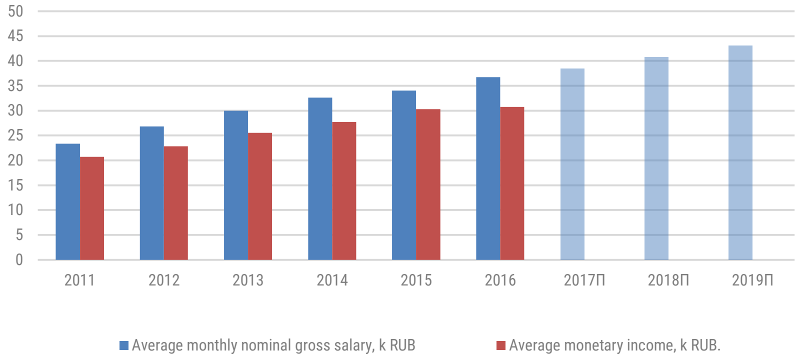
- According to the MED's baseline outlook, the level of gross disposable household incomes will decrease to **59.4%** of GDP by 2019 (in 2016 – **61.4%** of GDP), while the bulk of the reduction will be in 2019.
- The share of net property income received by households during 2017-2019 will remain positive and rise slightly (to **2.8%** against **2.6%** of GDP in 2016).
- By 2019, the rate of household savings will decline to **11.1%** of their gross disposable income from **12.3%** in 2016 (from **7.6%** to **6.6%** of GDP, respectively). The share of disposable income spent on current needs will increase to **88.9%** by 2019 relative to **87.7%** in 2016.
- According to the outlook of the Ministry of Economic Development, the share of household consumption spending in GDP will decrease to **53%** of GDP (compared to **54%** of GDP in 2016) against the backdrop of slow growth in real disposable incomes.

Outlook for the dynamics of real wages and real personal incomes, %



Source: RSC, EMR

Outlook for the dynamics of the nominal gross wages and average personal incomes



Source: RSC, EMR

STRUCRURE PART VII

Scenario conditions and economic growth highlights in Russia
Scenarios of food retail market growth by INFOLine
Outlook for personal income and spending
Outlook for retail turnover
Outlook for food retail market growth
Outlook for food retail turnover by sales channels
Outlook for the number and space of facilities by food sales channels

3 scenarios for the development of the industry

7 slides, 10 diagrams

SOURCES

- The FSSS of the Russian Federation. Socio-economic situation in Russia. January-February 2017 / March 21, 2017 (Bulletin).
- The FSSS of the Russian Federation. Special issue of the report “Socio-economic situation in Russia” for 2016 // April 14, 2017 (Report)
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