

# Sanctions Spark Russian Cheese Industry Boom

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Profits at Russia's cheese factories are booming as state support and bans on imports from the West force supermarkets to turn to local producers.

Cheese shelves at Russian supermarkets that were filled with foreign brands were hit hard when Moscow in August retaliated against Western sanctions over the Ukraine crisis by barring a range of food imports from the United States, European Union and a handful of other countries.

"Eighty percent of our cheese lineup has changed this year," said Andrei Golubkov, press manager at high-end supermarket chain Azbuka Vkusa. "We now have four times more made-in-Russia cheese," he said.

New demand from retailers has stimulated local supply: Cheese production in Russia increased by 29.5 percent between January and April, compared to the same period in 2014, reaching 180,000 tons, according to data from state statistics service Rosstat.

But there is a dark side to the boom: Rosstat data show that production of "fake" cheese, where palm oil is used as a cheaper milk substitute, is also rising fast, thanks to poor regulation and Russians' preference for cheap goods.

## **Profits Rising**

One company that is cashing in is the Sernursky cheese factory in Yoshkar-Ola, a city of 250,000 halfway between Moscow and the Ural Mountains.

"Before the embargo we sold two tons of Maasdam cheese to Moscow retailers per month. Now we sell 3 1/2 tons," said Konstantin Glazhenkov, the factory's deputy sales director. The company supplies big Moscow supermarkets like Sedmoi Kontinent, Azbuka Vkusa, Auchan and Metro.

The Sernursky factory also recently launched production of new cheese: halloumi.

"Since Cypriot cheese is not being delivered to Russia anymore, we are planning to occupy the niche," Glazhenkov said. As part of the expansion, his company this year opened an office in Moscow, he said.

Sernursky is not the only one to see business boom. Neva Milk, a St. Petersburg-based cheese factory that produces 2,000 tons of dairy goods per year, saw profits rise 25 percent in the first quarter of this year, compared to the same period in 2014.

Flush with cash, the company also opted to produce a new type of cheese that it said had never before been mass-produced in Russia.

"In September, just after the bans, we opened a new factory to produce Feta, a traditional Greek cheese," said Maxim Malygin, Neva Milk's vice president for strategy and investment.

The factory in the Vologda region north of Moscow can produce 450 tons of cheese per month, he added.

Even falling milk production — which declined by 0.5 percent in the first four months of this year compared to the same period in 2014 — is not halting cheesemakers. The shortfall has prompted some factories to take matters into their own hands. The Sernursky factory, which saw its first quarter profits rise by 15 percent year-on-year, has 4,000 goats and uses milk from its own farm.

## **Supermarket Scramble**

While the import bans opened opportunities for producers, retailers scrambled to respond.

"We had to replace around 350 cheese brands after the embargo," said Azbuka Vkusa's Golubkov.

Maria Kurnosova, public relations manager at the Russian subsidiary of French hypermarket chain Auchan, said the company's imports of cheese to Russia had fallen sharply. She said Auchan was now importing 25 percent of its cheese, mainly from Belarus, Argentina, Serbia, Uruguay and Switzerland, which were not affected by the bans. She could not say what proportion of cheese had been imported before the embargo.

Auchan, which sells mostly to low- and middle-income Russians, said its most popular cheese is the Russian "Lamber," a semi-firm cheese produced in the republic of Altai in southern Siberia at the Rubtsovsky dairy factory. PepsiCo, which owns the factory through the Russian food company Wimm-Bill-Dann, said last month it planned to boost production capacity of Lamber by 40 percent.

At Azbuka Vkusa, which caters mostly to rich Muscovites, the best-selling items are still brands from Switzerland, as well as Italian and French lactose-free cheeses that were not banned.

## **Palm oil**

"Auchan customers prefer domestic cheese because it's cheaper," Kurnosova said.

Local cheese has become less expensive than imported products thanks to last year's sharp devaluation of the ruble. But another factor is that some producers are substituting milk for cheaper palm oil in cheese production.

According to Rosstat, imports of palm oil to Russia rose by 37 percent year-on-year in January and February this year.

"Palm oil is very actively used in food production in Russia," said Alexei Alexeyenko, assistant to the head of Russia's Federal Service for Veterinary and Phytosanitary Surveillance, or Rosselkhoz nadzor.

Alexeyenko said that some types of palm oil can harm the cardiovascular system and deplored a lack of regulatory oversight. "There is no unified food quality control in Russia to provide absolute safety from field to [supermarket] shelf," he said.

The Sernursky factory's Glazhenkov said the rise of palm oil was hitting business: "The market is flooded with producers offering products with the name 'cheese' on them. They are selling for 35 percent less than our cheese, which forces us to lower our prices as well," he said.

This increased competition has put honest producers in a bind. To take advantage of the opportunities offered by the embargo on Western imports requires investment, but dishonest rivals create pressure to slash prices.

In such circumstances, Glazhenkov is glad for state support. Russian officials trumpeted the embargo on Western food imports as an opportunity to revive local agriculture, and tens of billions of rubles were dispersed last year.

"This year we are getting a state grant. ... We are going to raise sales in Moscow up to 12 tons by this fall," he said.

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