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Ice-Fili (АЙС-ФИЛИ)

You cannot defeat a nation that enjoys ice cream at minus 40 Celsius.

—Winston Churchill

To survive in Russia's ice cream industry during the 11 years since the collapse of the former Soviet Union was no small feat (see **Exhibits 1 and 2**). To be successful in these turbulent times was nothing short of amazing to industry observers. In 2002, Ice-Fili, a mid-sized Russian company with more than \$25 million in sales, was Russia's top ice cream producer. Surprisingly, it had outlasted several well-known international companies such as Ben & Jerry's, which exited the Russian market in 1997, and Unilever, which left in 2001. Ice-Fili had not only successfully transitioned from the tight controls of the Soviet regime to the infant Russian open-market economy in 1992, but it had also successfully navigated its way through the difficult times of Russia's 1998 financial crisis.

Ice-Fili was fighting to maintain its market share leadership in the increasingly competitive Russian ice cream market, which had decreased over the past few years to about a half-billion dollars in sales. Nestlé, which advertised heavily, was Ice-Fili's fiercest competitor. While most ice cream producers were left to fight in an already saturated ice cream kiosk system, Baskin & Robbins and Haagen-Dazs¹ had positioned themselves as premium ice cream producers, distributing through franchised restaurant and café networks. At the other end of the competitive spectrum, the small regional ice cream producers, which were believed to have lower production costs than Ice-Fili and other Moscow-based producers, were now making strong inroads in the major metropolitan markets.

Anatoliy Shamanov, Ice-Fili's CEO, wrestled with some fundamental strategic questions: Could Ice-Fili maintain its market lead over Nestlé? Should Ice-Fili invest in its own chain of cafés in order to find new retail avenues for its ice cream products? How could Ice-Fili compete with regional producers without engaging in a price war? And how could Ice-Fili attract the talent necessary to manage in a competitive market economy?

Consumption of Ice Cream in Russia

There are many stories explaining how the Russians came to love ice cream. According to one story, Czar Peter the Great brought ice cream back from France in the seventeenth century; yet another claimed that ice cream achieved its popularity after the Bolshevik Revolution in 1917 when it became available to the masses and not just the noble classes.² Another Russian ice cream legend

Professor Michael Rukstad, Research Associate Sasha Mattu, and Asya Petinova (MBA '02) prepared this case. HBS cases are developed solely as the basis for class discussion. Cases are not intended to serve as endorsements, sources of primary data, or illustrations of effective or ineffective management.

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maintained that ice cream sellers were as numerous in winter's subzero climate as they were in the summer. According to a Baskin-Robbins manager in Russia: "Russians eat even more in the winter, although it sounds strange. Perhaps it's because in summer it melts by the time you get it home. In winter you can eat it as long as you want."³

Despite those casual observations, industry statistics indicated that Russian ice cream consumption peaked during the summer months, exhibiting strong seasonal differences (see **Exhibit 3**). In 2001, Russians consumed 2.5 kilograms of ice cream per capita, compared with the 16 kg consumed in the United States, 17 kg in France, and 18 kg in Canada.⁴ Ice cream was considered primarily as an inexpensive snack consumed "on the go," resulting in a greater number of spontaneous purchases from kiosks or street stalls than from supermarkets and grocery stores (see **Exhibit 4**). According to a Russian business analyst: "Domestic [Russian] manufacturers have done little to position ice cream as a family product, being satisfied with spontaneous, impulsive consumption. Ice cream is not an expensive product, and many people can afford it. But people still don't consider it to be something they can have at home for dessert."⁵ In contrast, over a third of the \$20 billion U.S. ice cream market was from in-home consumption.

Traditional Russian ice cream contained about 15% milk fat, compared with the 10% found in premium western brands (see **Exhibit 5**). This contributed to the unique flavor of Russian ice cream,⁶ which was less sweet and more aerated than the typical ice cream product of the U.S. and Europe (reminiscent of whipped cream). Also, traditional Russian ice cream was made with all natural ingredients and did not contain preservatives. It was believed that Russian consumers were generally more concerned about preservatives in food than fat levels. According to an industry trade association representative, "Millions of foreigners, after arriving in Moscow and tasting our ice cream, have proclaimed Russian ice cream to be the best in the world."⁷

In the selling of ice cream, many products competed for the consumer dollar, including beer (Baltica and dozens of other domestic brands), soda (primarily Pepsi and Coke), yogurts, chocolate (Mars, Nestlé, and numerous domestic players such as Red October), and other confectionary candies. The producers of these products often spent considerably more on advertising than ice cream producers.⁸ In 2001, ice cream producers spent less than \$5 million on advertising in Russia (1% of sales), while the \$4.5 billion Russian beer market spent approximately \$90 million (2% of sales) and the soft drink industry spent almost \$200 million (7% of sales) on advertising.⁹

The beer, soft drink, and confectionary industries enjoyed increasing market demand rather than the depressed trend found in the Russian ice cream industry. In 2000, the production of ice cream was down 3.5% from the year before; in contrast, the production of confectionaries was up 8%, soft drinks 25%, and beer 23%.¹⁰ One industry expert sighed: "Nowadays, students prefer beer to ice cream."¹¹ The Russian beer market had grown 20% to 25% annually from 1997.¹² Russia had more than 300 breweries, which met 99% of the domestic beer demand.¹³

Russian Challenges

Prior to the dissolution of the Soviet Union in 1991, the state controlled all planning, production, and distribution of food products—ice cream was no exception.¹⁴ At the end of the 1980s, ice cream capacity increased substantially when the president of the Soviet Union, Michail Gorbachev, re-assigned alcohol factories to the production of ice cream as part of his anti-alcohol campaign.¹⁵ This decision resulted in the addition of 25 newly dedicated ice cream factories, bringing the total to 76 factories. The Russian ice cream industry produced 468,000 tons in 1990—the peak production year—out of almost 800,000 tons in the USSR as a whole. But within the next decade, ice cream companies

in Russia would suffer through two severe economic shocks that reverberated through all industries in the former Soviet Union.

Open market By the end of 1991, the political and economic situation had become so unstable that the Soviet Union was dissolved. Boris Yeltsin became the president of Russia, the largest of the newly independent republics. Over the next two years, Russia made a pointed shift from a state-run economy to an open-market economy that encouraged free enterprise and competition through privatization and price liberalization.¹⁶ In the process, there was a dramatic drop in ice cream production; in 1991–1992, output fell to levels last experienced in the early 1970s. Foreign ice cream companies, including Ben & Jerry's, Baskin & Robbins, Nestlé, and Unilever, all poured into the Russian market to capitalize on the open-market opportunity.

For domestic producers, including Ice-Fili, these economic changes led to a temporary paralysis. Under the state-run system, these companies focused on the manufacturing and storage of ice cream and were not responsible for other activities in the value chain. Moreover, with their large freezing capacities and manufacturing capabilities, they were also involved in the storage and wholesale of meat, milk, and fish products. When the markets opened, domestic producers required significant financial investments to update production technology, modernize infrastructure, develop better marketing and packaging solutions, develop dealer and distributor networks, and create new distribution channels. Some manufacturers partnered with local distribution companies, which in turn became part shareholders. Some resorted to selling foreign ice cream products or expanded into new markets such as the production of butter, mayonnaise, bread, fish, sausage, and confectionary to compensate for their dwindling revenues.

Financial crisis of 1998 The industry again took a turn for the worse when Russia defaulted on its debt payments in August 1998, resulting in a financial collapse and devaluation of the ruble by two-thirds. Many foreign companies dramatically reduced their imports into the Russian market because Russian consumers could no longer afford imported goods.¹⁷

Some foreign competitors, such as Nestlé, which had already invested in local production plants by 1997, managed to ride out the crisis by boosting local ice cream production instead of importing their global brands. But most new investors felt that the Russian market was just too risky and stayed away.¹⁸ The crisis also affected domestic ice cream manufacturers, which had to reduce quickly their reliance on imported materials used in their ice cream production. During the crisis period, ice cream imports into Russia dropped from 19,000 tons to 6,000 tons per year, whereas exports started growing (see **Exhibit 6**). By 2000, Russia was exporting more than 11,000 tons of ice cream, mainly to former states of the Soviet Union.

Ice-Fili

There is a Russian saying, "A bad soldier is one who does not dream of becoming a general." Even small companies dream of becoming large someday.¹⁹

—Shamanov

In 1937, the Soviet government established the company "Moshladokombinat N 8" (today Ice-Fili) on the outskirts of Moscow. It became the first large-scale industrial Soviet ice cream manufacturer, producing as much as 25 tons of ice cream a day (the second-largest ice cream factory in the world, after a factory in Boston). Over the next six decades, the factory underwent three major equipment modernizations and was capable in 2001 of producing 200 tons of ice cream per day. One-fifth of its total output was sold in Moscow (see **Exhibit 7** for company financials).²⁰

Anatoliy Vladimirovich Shamanov joined Moshladokombinat N 8 in 1968 after graduating from the Leningrad (today, St. Petersburg) Institute of Technology, having specialized in refrigeration and compressor tools and equipment.²¹ Shamanov left in 1974 and served in a variety of positions at other specialized frozen-food and ice cream companies before rejoining Moshladokombinat N 8 in 1988 as the CEO.

The company was privatized in 1992 as a private joint-stock company and rechristened “Ice-Fili.” Shamanov lead Ice-Fili through the laborious restructuring process necessary to make the company competitive in the new market economy. Commenting on the challenges, he reflected: “We had to change everything—our technology, our packaging, our way of doing business. But the most difficult and important aspect was changing our psychology. We had to adjust to the fact that nothing was going to be simply given to us anymore. We were in a free float and had to survive on our own without anybody’s help. Some people could not adjust to this and left.”

Product Russian ice cream makers produced a relatively small number of ice cream products, predominately in vanilla and chocolate flavors. They were typically single-portion sizes packaged as snacks, designed to be sold from refrigerators in kiosks and stores to customers as they walked by. According to Russian marketing experts, Russian producers made only 240 different ice cream-related products, while Baskin-Robbins alone in the U.S. offered 650 varieties.²² In 2002, Ice-Fili offered 170 different ice cream products (see **Exhibit 12**). Every year Ice-Fili added about 20 new products, which typically involved the modification of traditional recipes or more advanced add-ins, such as candy-coated ice cream that exploded in the mouth.²³ Other Ice-Fili product innovations included a diabetic ice cream reintroduced in 1998 for the 140,000 diabetics in Moscow alone and, in 2002, its first ice cream product with American-style taste and texture (vanilla with dried fruit) for at-home consumption in Russia.²⁴ Also that year, the Moscow World Food Exhibition awarded Ice-Fili with a silver medal in the “Product of the Year” category for “Eralash” (an ice cream product that featured milk-glazed crème-brulé with corn chips). Ice-Fili was the only ice cream company that received an award.²⁵

The company’s flagship ice cream brand, introduced in 1964, was “Lakomka,” a cylindrical ice cream snack with a whipped chocolate glaze. Lakomka was still one of the three most recognized brands of ice cream in Russia and, by 2001, was responsible for 30% of Ice-Fili’s sales volume.²⁶ However, because of Lakomka’s Soviet legacy, Ice-Fili could not register it as its own trademark; thus, in the late 1990s, at least five other companies started producing Lakomka. Leningradskoe, a briquette-shaped vanilla ice cream with a chocolate glaze, was another well-known Ice-Fili product, but many Russian domestic companies produced this product too. Besides these generic products, other traditional Ice-Fili brands included Batonchiki-Fili, which accounted for a significant share of Ice-Fili’s sales.

In 2002, domestically produced Russian ice cream was among the cheapest in the world to buy.²⁷ Ice cream prices ranged from 2.5 rubles (8.5 cents) to 15 rubles (about 50 cents) per portion. Ice-Fili priced its ice cream products at approximately 6 rubles, placing it in the medium-level category; Nestlé positioned some of its brands in the premium ice cream category at 10 rubles (or more) per product, while the regional producers filled the low-price category at 3 to 4 rubles.²⁸ According to an Ice-Fili executive: “A 10% change in retail price won’t make much of a difference in consumer’s purchasing behavior, but a 50% change would. There are only slight seasonal changes in price.”²⁹

In 2002, the popularity of bulk ice cream sold in boxes, containers, and buckets increased significantly in the major metropolitan areas as the home consumption segment of the market became more important. Traditional single-portion snacks remained the dominant segment in less wealthy regions.

In order to continue making profits during stagnant periods and to reduce overall product cost, many domestic refrigeration companies and ice cream producers leveraged their infrastructure, production facilities, and cold-storage facilities to diversify their operations by producing other products such as frozen food and meat.³⁰ Ice-Fili had a limited production of mayonnaise and other fat-containing products, as well as glaze for ice cream.³¹

Manufacturing

Ice cream production varied based on seasonal demand, and the average high-season production level was approximately three times the average low-season production level. The production volume could vary between 10 tons to 150 tons per day.³² In 2002, the estimated manufacturing capacity of the Russian ice cream industry as a whole ranged from 500,000 to 880,000 tons a year.³³ However, the production volumes were significantly lower. In addition, the ice cream production process in Russia differed from that in the U.S. (see **Exhibit 8**).

In 1999, the profit margins for ice cream production were estimated to be 15%–20%, down from the 30%–40% range realized in 1998. However, this margin was high even by Russian food industry standards where, for example, the comparable profitability in the confectionary industry in 1999 was 6%–8%, down from 14% in 1998.³⁴

Ice cream in Russia was subject to a value-added tax. This was increased from 10% to 20% at the beginning of 2000, when ice cream was reclassified as a luxury product. Many ice cream producers attempted to lobby for a return to the 10% tax bracket for ice cream, arguing that all ice cream ingredients are “socially important foods” subject to a VAT of 10%.³⁵ Shamanov commented on the effects of the increased VAT: “Enormous funds were diverted from investment projects to tax payments.” In July 2000, VAT was decreased to its previous 10% level for milk-based ice cream products but remained at 20% for fruit-based ice creams and ice popsicles.³⁶

Ice-Fili, like other domestic ice cream producers, was affected by the downward trend in consumer demand in Russia. In 2000, it produced 20,000 tons of ice cream compared with 27,500 tons in 1998 (see **Exhibit 1c**). The company’s exports accounted for less than 1% of sales in 2000.³⁷ These exports were mainly to former Soviet states, eastern Europe, and Israel, for which Ice-Fili had a special kosher ice cream. In 2001, Ice-Fili’s exports increased marginally to 12 tons of ice cream.³⁸

Ice-Fili employed approximately 550–600 people at its Moscow-based factory of whom 200 were seasonal workers. More than 40% of the employees had been working there for more than 20 years.³⁹

Raw materials The major ingredients of Russian ice cream were condensed milk, milk powder, sugar, butter, and flavor additives (for a breakdown of relative costs of ice cream ingredients refer to **Exhibit 9**). Carbohydrates such as sugar constituted about 15% of the product volume (higher in sorbets and fruit ice creams); proteins from condensed dry milk and other milk products constituted 10%; fats from butter, milk products, or palm oil varied depending on the type of ice cream (15% for Plombir ice cream, 10% for cream ice cream, and 5% for milk ice cream); and the balance was non-nutritional and filler components such as water.⁴⁰

The use of varying percentages of milk fat affected the palatability, smoothness, consistency, color, texture, digestibility, and energy value of the finished product.⁴¹ A producer could use a variety of dry milks varying from 1.5% to 25% fat and from 27% to 98.5% protein. Following the legacy of the traditional Russian ice cream makers, Ice-Fili prided itself on using only high-quality natural ingredients, eliminating the use of any artificial preservatives or colorants. Instead of using all milk-based ingredients, some ice cream producers, including Nestlé, chose to use palm or coconut oil and

preservatives as cost-saving alternatives. According to Andrei Kabuzenko, Ice-Fili's commercial director: "Changing these ingredient parameters may reduce costs, but the taste would be affected. In the case of producers who use additives, the taste could be corrected since there is even a creamy flavor additive, but for Ice-Fili, which doesn't use additives, the quality of our ingredients becomes more important."⁴²

Foreign producers used chemical preservatives to increase the shelf life of their ice cream products from about 6 months to as much as 18 months. However, the traditional Russian ice cream manufacturers exclusively used all natural ingredients. While this made Russian ice cream superior in quality, it did not keep as well. Consequently it was difficult to store and transport, thus increasing overall costs.

During the early 1990s, Russian ice cream producers had to rely on imported raw materials. They could not depend on the quality or quantity of ingredients from domestic sources and imported everything from the wooden sticks for the ice cream to disinfectants used in manufacturing plants.⁴³ Shamanov commented: "Effectively, the Russian ice cream industry was investing abroad rather than at home."⁴⁴ This dependency on import sourcing varied across companies, but the Moscow ice cream companies were reputed to have imported more than 50% of their equipment and food components.⁴⁵

Following the 1998 devaluation, the competitive situation had changed, and Russian producers relied much more on local suppliers for their raw materials. An important exception for Ice-Fili's ice cream was sweet cream butter with 82% fat content, which was imported from New Zealand in order to achieve the necessary fat levels (because Russian butter contained only 72% fat). Other imported inputs were packaging materials from Italy, stabilizers from Denmark, and coconut oil for hardening of the chocolate ice cream coating.⁴⁶ Ice-Fili used three to four suppliers for each of its major ice cream ingredients. According to Kabuzenko: "It is not a problem to find a new supplier since we constantly receive offers from new ones."⁴⁷ The prices of domestically sourced ingredients tended to fluctuate significantly over the year—the highest were at the beginning of May and the lowest at the end of August. For example, a kilogram of milk powder fluctuated from a high of 52 rubles to a low of 28 rubles, and a kilogram of sugar fluctuated between a high of 12 rubles and a low of 9 rubles.⁴⁸

Equipment and technology In the early 1990s, the Russian ice cream industry severely lagged behind its western counterpart in technical capabilities in production, ingredient use, and packaging. Alexander Kladiy, chief production specialist of Ice-Fili, estimated that by the beginning of the 1990s most Russian firms were about 40 to 60 years behind the world's technology level.⁴⁹ Experts argued that the leading companies in the Soviet ice cream industry had initially developed in stride with the United States, having imported most of their manufacturing equipment from the U.S. from the 1930s to the 1960s. However, in the 1960s and 1970s, Russian standards as a whole fell noticeably behind worldwide industry standards.

According to Zoya Marakova, Ice-Fili's production facility manager: "[Ice-Fili] is the only one that can make machinery as old as this work as well as it does."⁵⁰ Ice-Fili spent significant sums of its internally generated cash flow in the late 1990s for modernization, overhaul, and expansion. Shamanov noted: "Over the last two years, the company has pumped in \$8 million from its own pockets."⁵¹ In 2002, most of Ice-Fili's ice cream production relied on its newly imported equipment. The exception was four of Ice-Fili's traditional ice cream products that had been introduced to the market during the Soviet era. These four brands were still produced using the older-generation equipment and accounted for 25% of Ice-Fili's overall production capacity.⁵²

The major suppliers of Ice-Fili's ice cream equipment were Danish and American firms because Russian ice cream equipment was still of low-quality, narrow assortment and lacked flexibility to be

used for production of various types of ice cream.⁵³ In 1999, 90% of the equipment used by Russian ice cream manufacturers to produce and sell ice cream was imported.⁵⁴ The machinery used for freezing and packaging, in particular, was highly specialized equipment, costing \$1.5 million to \$2 million per complete production line.⁵⁵

However, the local supplier base was developing fast. Some new companies manufacturing ice cream production equipment were born from military conversion efforts. Some defense companies in search of new orders turned to ice cream producers. They started by modernizing old equipment but then continued by developing totally new equipment. The development was jointly financed by ice cream producers. In 2001, there were at least 10 private ice cream equipment companies in Russia, Ukraine, and the Baltic countries.

Distribution

In 2001, there were five retail channels for ice cream in Russia: kiosks, minimarkets, traditional grocery stores called “gastronom,” supermarkets, and restaurants (see **Exhibit 10**).

Kiosks were the largest channel and accounted for 49% of the overall ice cream distribution. Ice cream kiosks were small boothlike structures where transactions were conducted through small windows.⁵⁶ There was typically very little, if any, storage space and precious little room for the seller to sit. They typically carried a very narrow range of ice cream types. The numerous kiosk locations in metropolitan areas promoted impulse ice cream purchases. In 1999, Moscow had about 11,000 ice cream outlets, of which 1,600 were ice cream-only kiosks. According to an industry observer: “The street market in Russia, particularly in Moscow, is already saturated with kiosks selling ice cream on every street corner.”⁵⁷ Most domestic competitors fought for their market share through the kiosk system.

Minimarkets, accounting for 29% of ice cream sales, were slightly larger than kiosks but still capitalized on impulse purchases since they were conveniently located near subway stations and were particularly common in larger Russian cities such as Moscow and St. Petersburg. They had a limited range of food and drinks and were comparable to convenience stores in America.

Gastronom were characterized by the counter-service system where purchases for different product groups (meat, dairy, etc.) were made separately at designated counters within the store. In the more remote and less wealthy areas, gastronom were still the dominant retail chain. Overall, gastronom accounted for about 17% of Russian ice cream consumption.

One of the fastest-growing channels that emerged in the late 1990s was supermarkets, which were gradually replacing gastronom in the major cities such as Moscow and St. Petersburg. Despite their growth, they were still small (around 2% of total ice cream sales in 2002). The majority of the large supermarkets were Russian companies, but by 2002, major international chains, such as SPA of the Netherlands and Metro of Germany, had also entered the Russian market or had announced their decision to do so.

In an effort to reach the impulse consumer during the summer months, gastronom, minimarkets, and kiosks all put ice cream carts on the streets. Many producers also provided retailers with branded refrigerator displays to hold their products, but often, retailers used these displays to hold competitors’ products and other frozen foods as well.

The other small retail channel was restaurants and cafés, which were dominated by foreigners such as Baskin & Robbins and Haagen-Dazs. Domestic competitors had yet to compete successfully in this area, though industry experts felt that this was a large untapped segment. Approximately 30%

of ice cream sales in the West were carried out in restaurants and cafes, yet this segment only accounted for about 3% of the ice cream sales in Moscow, with a higher proportion in Moscow and St. Petersburg and considerably less in the more remote regions.⁵⁸ In 2002, Ice-Fili also began supplying the Pizza-Hut restaurant chain in Russia with its ice cream products.

In 2002, 80% of Ice-Fili's ice cream distribution occurred through kiosks and minimarkets. Ice-Fili contracted with dozens of companies, such as Eskimo-Fili, which typically had their own kiosks and carts and hired their own people to staff them.

Ice-Fili also relied on the services of dozens of other small distribution companies, such as Service-Fili, an affiliated but independent distribution company responsible for delivering approximately 15% of Ice-Fili's total ice cream products to gastronoms and minimarts. Service-Fili owned its own refrigerators and trucks carrying the Ice-Fili logo. According to Alexdander Grigas, the CEO of Service-Fili: "Our deliveries are mostly to Moscow and we are not exclusive. On the same truck we carry approximately half Ice-Fili products, a quarter of one competitor's product, and a quarter of a second competitor's product."⁵⁹ Service-Fili would on average service 250 points of sale per day and about 2,000 total in Moscow. Of these, 100–200 were restaurants, 100 schools (which they were exiting because of low profitability), 300 gastronoms, and the remainder minimarkets.⁶⁰ These distribution companies relied on the provision of additional services in order to secure and maintain contracts. For example, Service-Fili offered ancillary services such as promotion of ice cream brands and point-of-service materials.⁶¹

In addition, Ice-Fili used companies such as Alter-West and Inka, which distributed to regional warehouses. For these companies, ice cream made up only 10% of their distribution volume. The remainder was the distribution of other frozen-food products.

Traditionally, Ice-Fili had not participated in distribution activities because of the huge capital investment and economies of scale required to develop these networks. According to Ice-Fili's directors, this was one area that was critical to success in the future. According to one director: "Although Ice-Fili has the greatest variety of products compared to the handful of Nestlé products, there is twice the likelihood of finding a Nestlé product rather than Ice-Fili's product in Russia. Distribution will be the new battlefield—availability of the product will be key."⁶²

Marketing

Historically, Russian ice cream producers had not needed to perform extensive marketing or advertising activities. However, the opening of Russian markets in 1992 created an opportunity for foreign companies to leverage their rich marketing experience from abroad and invest in building their brands in Russia. Nestlé and Mars (particularly in the confectionary industry) were quite successful in their use of this strategy.

The early success of these multinationals highlighted the inexperience of domestic producers. According to one industry observer: "The old type of managers [of Moscow-based producers] think that if they start a new line, or new type of ice cream, the business will grow for sure without even trying to study potential demand and competition. As a result, periodically there is overcapacity, and factories stay half busy for several months or do not work at all. More precisely, marketing is absent. It is one of the weakest parts of domestic manufacturers."⁶³

The ice cream industry exhibited a similar trend seen in other consumer goods industries in Russia where 90% of the companies spent the majority of their marketing dollars on TV advertising. Foreign multinationals, such as Unilever or Nestlé, accounted for as much as three-quarters of the

annual TV advertising in the ice cream industry. Aware of its own shortcomings, Ice-Fili ran its first TV advertising campaign on two nationwide Russian TV channels and on the Russian MTV channel in 2001.⁶⁴ Though Ice-Fili acknowledged that this was a step in the right direction, the ads barely mentioned either the company name or products.⁶⁵ According to Ice-Fili's marketing director, Alexei Grekov, Ice-Fili had only recently begun to develop marketing strategies, specifically how to target the company's products to the appropriate market group: "We have 170 different ice cream products. We really need to concentrate on minimizing the number of our products and focus on differentiating the products we already have."⁶⁶

Shamanov acknowledged that branding initiatives were intimately tied with Ice-Fili's new marketing focus: "Competitors are growing rapidly and these last two years have seen the number of new entrants increase especially from the southern regions and Siberia."⁶⁷ Given the predicted shift from kiosks and the consumer's impulse-buying habits to more family at-home consumption, Ice-Fili was optimistic in its abilities to reorient itself toward a more focused customer group in which it could leverage its role as the only traditional Russian all natural milk-based ice cream product. In 2001, Ice-Fili's marketing and advertising costs were estimated to be \$500,000 per year.⁶⁸

In an attempt to boost ice cream sales during the mid-1990s, Ice-Fili hired the Russian advertising agency Advice to develop new packaging for its products. Advice's designer developed Ice-Fili's new packaging in a 1950s style so that it would engender fond emotions in order to attract the consumer's attention.⁶⁹

Corporate Organization and Culture

Ice-Fili had a functional organizational structure: finance, production, commercial, technology, and reward systems (or human resources).

Since 2000, corporate focus had been on restructuring the organization to increase productivity and efficiency. Previously, Ice-Fili's operational structure was quite complex and inefficient. Also, fixed costs were very high, and Ice-Fili needed better processes that would spread out the costs over greater volume.⁷⁰ One example was pairing down the compensation structure for production workers from 117 different salary levels to one based on qualification, hardship/difficulty of work, health risks/hazards, overtime, and individual initiative. Under this new system, workers were penalized financially for tardiness, smoking, and other such infractions. Senior management's new compensation was a base salary plus a bonus, but with smaller premiums and larger penalties. Other organizational levers to reduce cost and increase production efficiencies included changing recipes, packaging, and waste processes.

According to Dmitri Pis'mennyi, Ice-Fili's financial director: "We need better control and management throughout our structural units. I believe that 80% [of our success] is establishing the right objectives, such as the right organizational chart, strategic business plans, and operational plans. But the importance is primarily on finding the right people, and establishing the right goals. There is a quote by Stalin that said: 'Human resource capital decides everything.'"⁷¹

In 2001, the company underwent several management changes. Alter-West, a distribution company that began distributing ice cream in 1992, had been a 37% shareholder in Ice-Fili.⁷² The initial partnership had allowed Ice-Fili to build quickly its distribution capabilities when the Russian markets were opened. By March 2001, however, through pressure exerted by Alter-West and the Moscow government,^a Shamanov was replaced by a former Alter-West director. A management

^a Various Russian government agencies took minority shares in most privatizations in the early 1990s.

struggle ensued that temporarily hampered Ice-Fili's production activities, but by July of that same year, Shamanov returned to his appointment as Ice-Fili's CEO. He also gained a controlling share of Ice-Fili.⁷³

The company constantly sought young, talented managers, many between the ages of 30 and 40, with an ability to thrive in an open-market economy. Ice-Fili's corporate culture could be best described as open and cooperative. Zoya Marakova elaborated: "We all work together. When we have any problem or issue, we all get involved in resolving it." In particular, there seemed to be a strong affinity toward ice cream among Ice-Fili's employees. Shamanov smiled: "Ice cream is a very sweet product. It causes smiles and makes people happy, and so, this naturally translates into our working environment."

Future growth Ice-Fili's directors faced the challenge of raising an estimated \$50 million capital necessary for financing future growth. These growth plans included diversifying geographically into eastern Europe and Germany and also potentially taking advantage of a "cash cow" opportunity for producing dry ice and selling it abroad for construction purposes, medical uses, and beverages such as beer, Coke, and Pepsi. Shamanov hoped to continue building on the company's small family culture. Ice-Fili's financial director, however, hoped that perhaps Ice-Fili might consider an initial public offering at some point but felt that it was currently a long way from that goal: "Ice-Fili's main concern is getting in shape to go to the market for public bonds sometime next year. We are looking to establish ourselves with more standards that are common in the West, such as the adoption of the ISO 9000 international standard."⁷⁴

Ice-Fili was not optimistic about introducing its ice cream products into the West. Currently it only sold a small offering of its products in California. Ice-Fili felt that there was still too much of a difference between Russian ice cream standards and those preferred by western consumers.

Competitors

In 2002, rivalry flourished among regional, Moscow-based, and multinational ice cream producers (see **Exhibit 11**). The industry grew from almost 100 companies in 1996, to 150 companies in 1998, to 300 producers by 2002. Ice-Fili remained the largest competitor in the domestic group with about 5% market share in 2002, though its share had fallen in recent years owing to new production facilities at dairy companies and private companies (see **Exhibit 1b**).⁷⁵

The Moscow-based ice cream producers banded together to form the Association of Russian Ice Cream Producers in 1998 in an attempt to pool resources and improve consumer demand for ice cream. Initially it consisted of only five members from Moscow, Kolomna, St. Petersburg, and Krasnodar, but by 2000 it had 32 companies including Ice-Fili, Service Kholod, and Metelitsa.⁷⁶ One of the group's primary goals was a joint marketing campaign, where all their products would be united under one brand name and logo.⁷⁷

In 1999, the association took the initiative to redefine GOST, a minimum state standard that determined ice cream classification, input composition requirements, and methods for evaluating quality. The objective was to ensure that the consumer was not misled by the use of milk and butter substitutes. According to one executive of the association:

In Soviet times, we had a quality system in the form of technical requirements that kept the quality high. We [the association of producers] will strive to ensure that a new GOST [state] standard would make it clear to the consumer what ingredients are in the ice cream. If he wants an ice cream made with substitutes, that's his business. We just want to protect the

traditional quality of Russian ice cream and its producers. We want to revive prestige and to retain popularity of our ice cream.⁷⁸

The association also hoped that GOST would serve as a rallying point in criticizing imported ice cream brands that used more preservatives and less fat than Russian ice creams.

Regional Producers

Some experts felt that the greatest threat in the Russian ice cream market emanated from regional producers. Many of these regional players were newly established, did not have the heritage of an old management system dating back to Soviet times, and had new manufacturing facilities resulting in a significant cost advantage. Product quality was varied, as was packaging; indeed some producers distributed their products solely in waffle cones. The regional companies also took advantage of lower rents and labor costs, which further contributed to their cost advantages.⁷⁹

While the small, local, newly established ice cream makers offered a more limited range of products, they accounted for about 30% of the domestic market.⁸⁰ The dramatic increase in the number of regional producers was explained by the shrinking frozen-food imports market, which had been impacted by the 1998 crisis. Many former frozen-meat and -fish wholesalers found it relatively easy to set up for ice cream production since they already had cold-storage and production capabilities. As a result of their entry, ice cream production capacity increased in 1999 by 30% over 1997 levels.⁸¹ According to an executive of the Association of Russian Ice Cream Producers: "There's no longer a need to transport ice cream from, say, Kamchatka [in the Far East] to central Russia because there are local producers everywhere."⁸² While Moscow-based producers found themselves losing their market share in the capital as well as other regions in Russia, it was difficult for them to attribute it to a superior regional competitor. The association's executive director stated: "[While] it would be too much to say that Moscow-based ice cream manufacturers are being cornered by more successful competitors from the regions, they're feeling less comfortable as regional manufacturers' products become more competitive."⁸³

In addition, regional producers, hungry to increase their market share, were regarded as being more flexible. According to one distribution company: "Last year we couldn't agree with any of the Moscow-based producers about supplying us with berry-flavored ice cream. During the summer period this kind of ice cream was both inexpensive and the most popular. We ended up resolving this problem through regional producers. Next summer, three regional producers are going to supply us with this kind of ice cream."⁸⁴

By 2002, a few regional producers exhibited especially aggressive growth strategies not only in their local markets but also in Moscow and other metropolitan markets. Inmarko, a Siberian company that started as an ice cream distributor and retailer, established two manufacturing facilities and recently subcontracted manufacturing to another two factories. In addition, Russkii Holod, another regional producer coincidentally also based in Siberia, planned to open a new ice cream factory in Moscow by the end of 2002. The company already had 150 kiosks in Moscow, and industry experts forecasted this number to double relatively soon.⁸⁵

Foreign Companies

After the financial crisis of 1998, foreign companies either left, as did Ben & Jerry's, or became fully capable of domestic manufacturing through regional production plants, as did Nestlé and Baskin & Robbins.

Ben & Jerry's In 1992, Ben & Jerry's began a joint venture, Iceverks, to manufacture ice cream for the Russian market. In line with Ben & Jerry's social and economic mission, the venture was designed to encourage international cooperation and global understanding while also providing a model of a small-scale private enterprise.⁸⁶ They received funding from the U.S. Agency for International Development to help finance the venture, which was a 50/50 partnership between Russian investors and Ben & Jerry's.⁸⁷ A production plant was built in the region of Karelia, north of St. Petersburg because of its similarity to Vermont, the birthplace of Ben & Jerry's. The first ice cream "scoop" shop opened in the town of Petrozavodsk in 1992.

Ben & Jerry adapted their recipes to accommodate the use of local ingredients. This proved challenging as the milk, cream, and sugar was processed differently in Russia, giving the ingredients a different taste than what the producers were used to in Vermont. Large quantities of flavoring such as vanilla, chocolate, and coffee were imported from the U.S., but as the demand increased for Ben & Jerry's characteristic exotic mix in flavors, such as chocolate fudge brownie and apple pie ice cream, local versions of the inputs were sought and variations of the product emerged, notably, a Finnish sandwich cookie that was similar but replaced the Oreo cookies flavor found in the U.S.⁸⁸

In February 1997, five years after its move into Russia, Ben & Jerry's withdrew from its joint venture. The three reasons for its exit were the high operating costs, the lack of modern wholesale distribution systems in Russia preventing market-share expansion, and the limited local management resources.⁸⁹ According to Bram Kleppner, Ben & Jerry's manager of Russian operations, the venture never turned a profit.⁹⁰ While other international ice cream companies may have chosen to stay because of their high capital investments, Ben & Jerry's chose instead to accept the venture as a loss and donated its installed equipment.

Unilever In 1994, Unilever took over one of the oldest and most famous Russian producers of perfume and cosmetics and expanded operations to a full line of household products. It sought to gradually decrease imports while purchasing more supplies domestically in order to reduce production costs. It was not until 1998 that Unilever decided to dip into the Russian ice cream market with its launch of the Algida ice cream brand. Unilever was a leading ice cream producer in many other markets and typically strove to build the leading share wherever it operated. Unilever outsourced its ice cream manufacturing in Russia to two ice cream factories in Moscow, in addition to importing ice cream that it produced in its own factories in Turkey and Hungary. It was estimated that Russians consumed 1,000–1,500 tons of Algida per year. To distribute Algida, Unilever bought 3,000 kiosk stalls, one-third of which were in Moscow.⁹¹

Unilever sold 17 brands of ice cream in Russia.⁹² In 1999–2000, Unilever spent approximately \$6.2 million on Algida's promotional material and \$1.2 million on advertising its imported Vienetta brand of ice cream cake.⁹³ However, by February 2001, Unilever had practically withdrawn from the Russian ice cream market, halting all local marketing and production of ice cream. Some of its ice cream brands could still be found occasionally on the Russian market because local distributors directly imported them.⁹⁴

Unilever representatives dismissed its exit from the ice cream industry as an experiment, an opportunity "to study the Russian ice cream market." A more critical opinion came from competitors who felt that Unilever's failure stemmed from the poor distribution of its product. According to the representative of Unia-Trade, a Russian ice cream distributor, Unilever trusted distribution of its ice cream to a company that distributed other Unilever products but lacked the experience of working specifically with ice cream. According to other observers, many grocery stores during the prime summer months did not get Algida delivered on time and stuffed the products in competitors'

branded refrigerators.⁹⁵ Still others argued that Russian consumers tired of imported ice cream with its lower fat content and returned to traditional Russian ice cream products.

Baskin-Robbins Baskin-Robbins was founded in 1945 in Glendale, California, and became a wholly owned subsidiary of Allied Brewery in 1973, which was subsequently purchased in 1978 by Allied Domecq PLC, a London-based international food, drink, and leisure group. In 1986, Baskin-Robbins Incorporated was formed and included two new subsidiaries, Baskin-Robbins USA and Baskin-Robbins International. Baskin-Robbins was a pioneer on June 8, 1990, when it entered the Russian market by opening the first ice cream store with a sidewalk café (on historically well-known Arbat Street in Moscow) as a joint venture with Mosrestoranservis, a Moscow government entity that provided goods and services to Moscow restaurants. This deal was part of Baskin-Robbins' aggressive global expansion initiative, which included 3,500 stores in more than 44 countries.⁹⁶

Baskin-Robbins was the first American franchise operation in the Soviet Union to sell its products in Russian currency. In general, Baskin-Robbins offered 60 out of its 650 ice cream flavors to the Russian market. These included its traditional baseball nut, red raspberry cheesecake, and mint chocolate chip flavors.⁹⁷ Managers at Baskin-Robbins felt: "Once they have tasted our Pralines 'n Cream, Soviet life will never be the same."⁹⁸ The more expensive ice cream flavors that used alcohol and other expensive ingredients were not sold in the Russian ice cream markets.⁹⁹

The price for a single scoop of ice cream was 30 rubles, compared with 6–12 rubles for domestic ice cream bought at a kiosk. Baskin-Robbins was able to maintain its international brand appeal as well as prices that were significantly higher than traditional Russian ice creams. A company executive stated: "We use almost all imported ingredients, only the sugar is domestically produced. In the coming year [2001], however, Russian cream may be used if it reaches acceptable quality."¹⁰⁰

Similar to its operations in other countries, Baskin-Robbins flooded the Russian market through a franchising system whereby independent companies and entrepreneurs operated cafés and shops under the Baskin-Robbins brand name. By focusing on the restaurant/café segment of the Russian ice cream market, Baskin-Robbins enjoyed few (if any) competitors. Baskin-Robbins supported its franchisees in design, marketing, personnel training, and advertising. Typically, managers were trained at the Baskin-Robbins corporate training center and headquarters in California and given pretraining materials including videotapes, all prepared by Baskin-Robbins, but for the Russian franchises, managers were trained at specific locations.¹⁰¹ According to a Russian investor: "Russia definitely is lagging in the franchise business. But Baskin-Robbins, which was a pioneer in the franchising business worldwide, has managed to turn it into a success here. The secret of our success is the established know-how of Baskin-Robbins, our operator's knowledge of the Russian market and the willingness to take risks."¹⁰²

In May 1996, Baskin-Robbins launched production of ice cream at its new factory in Moscow, which cost \$30 million and had a production capacity of up to 16,000 tons of ice cream per year. It was one of the largest Baskin-Robbins factories in the world, and its capacity was enough to serve 1,000 Baskin-Robbins cafes. However, in 2001 its capacity utilization was only running at 7%–12%. The company franchisee network consisted of 105 cafes in approximately 35 cities in Russia and CIS.¹⁰³

Nestlé Henry Nestlé negotiated his first deal with Alexander Vencel, a St. Petersburg businessman, by the end of the nineteenth century, securing Nestlé as a dairy product supplier to the Russian Empire. This established Nestlé as the foreign ice cream producer having had the longest and most established relationship with Russia.

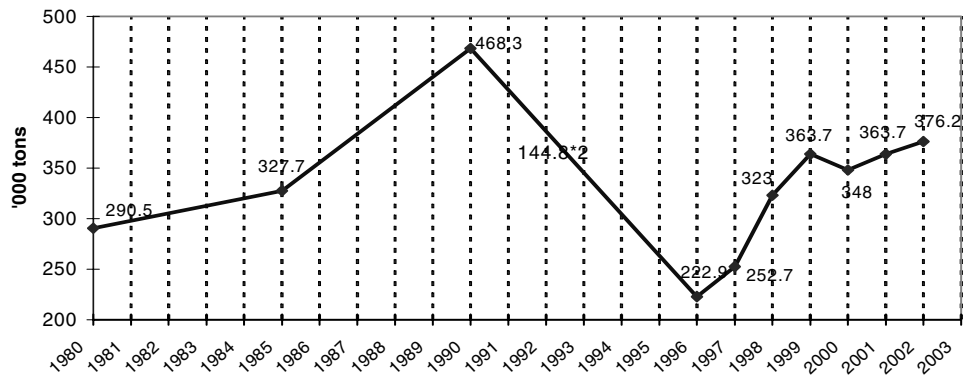
The Swiss food giant, continuing its long-term investment strategy, began actively investing in local production and development of food and beverage products that fit Russian tastes and traditions. It was conscientious about using locally supplied components for these products, a practice that ultimately sustained Nestlé during the severe Russian economic fluctuations that greatly affected other multinationals that had tried to enter the Russian market in the early 1990s. By having invested early in a domestic infrastructure, Nestlé developed its own independent storage facilities and distribution and marketing networks, which included kiosks and branded refrigerator displays. Nestlé's successful strategy in other countries was to maintain low production costs using local production for its heavily branded product.¹⁰⁴ It also made significant investments in training and development of its local staff.

Nestlé invested \$20 million in ice cream production between 1996 and 1999. In June 1996, Nestlé acquired a controlling share in an ice cream factory in the Moscow region. The factory produced 9,500 tons in 1997 and 13,000 tons in 1998. In June 1998, Nestlé made another acquisition—it bought a controlling share in an ice cream factory in Krasnodarskiy Krai (in the south of Russia).¹⁰⁵ Nestlé made significant capital investments in order to modernize and expand both plants and to develop their infrastructure and facilities to ensure that they met Nestlé's international manufacturing standards. In 2000, Nestlé had the second-largest ice cream market share after Ice-Fili and produced about 16,000–17,000 tons.

Nestlé produced nontraditional Russian ice cream (using both milk and vegetable fats) under new brand names such as “Eskimo Kimo” and “Rozochka” (see **Exhibit 13**) that cost between 8 and 13 rubles a portion (27 to 43 cents).¹⁰⁶ Most of its Russian brands were especially developed for the Russian market. For example, Nestlé's “48 Kopeek” product referred to a traditional Russian plombir ice cream product in briquettes of 250 grams that was popular in Soviet times and cost exactly 48 kopeek^b at that time. Nestlé actively advertised other ice cream brands such as “Extreme” and “Mega” through extensive TV campaigns.

One industry participant commented on Nestlé's strong presence in the Russian ice cream market: “I can tell you for sure that in two to three years there will be only one brand in the Russian market—Nestlé—unless we [domestic makers] combine our efforts in a struggle for that market.”¹⁰⁷ Many domestic ice cream producers feared the kind of domination that Nestlé showed in Egypt, where in only a matter of a few years, it had managed to oust 23 domestic ice cream producers to become the only ice cream producer left in the country.¹⁰⁸

^b There are 100 kopeeks to a ruble.

Exhibit 1a Ice Cream Production in USSR, 1980–2002**Ice-cream production in Russia, 1980-2002**

Source: Compiled from Ice-Fili documents and Goskomstat (Russian State Statistics Committee) data.

Exhibit 1b Production and Consumption of Ice Cream in Russia

	1980	1985	1990	1996	1997	1998	1999	2000	2001	2002
Production volume ^a (thousands of tons)	290.5	327.7	468.3	222.9	252.7	323.0	363.7	348.0	363.7	376.2
CAGR, %	N.A.	2.4%	7.4%	-11.6%	13.4%	27.8%	12.6%	-4.3%	4.5%	3.4%
Consumption volume (thousands of tons)	290.4	327.7	468.4	221.4	250.1	327.7	365.8	349.4	362.0	374.4
CAGR, %	N.A.	2.4%	7.4%	-11.7%	13.0%	31.0%	11.6%	-4.5%	3.6%	3.4%
Consumption per capita, kg	2.1	2.3	3.15	1.5	1.7	2.2	2.5	2.4	2.5	2.6
CAGR, %	N.A.	1.8%	6.5%	-11.6%	13.3%	29.4%	13.6%	-4.0%	4.2%	4.0%
Population, million	138.3	142.5	148.7	147.6	147.1	146.7	146.3	145.6	144.8	144.0
CAGR, %	N.A.	0.6%	0.9%	-0.1%	-0.3%	-0.3%	-0.3%	-0.5%	-0.5%	-0.6%

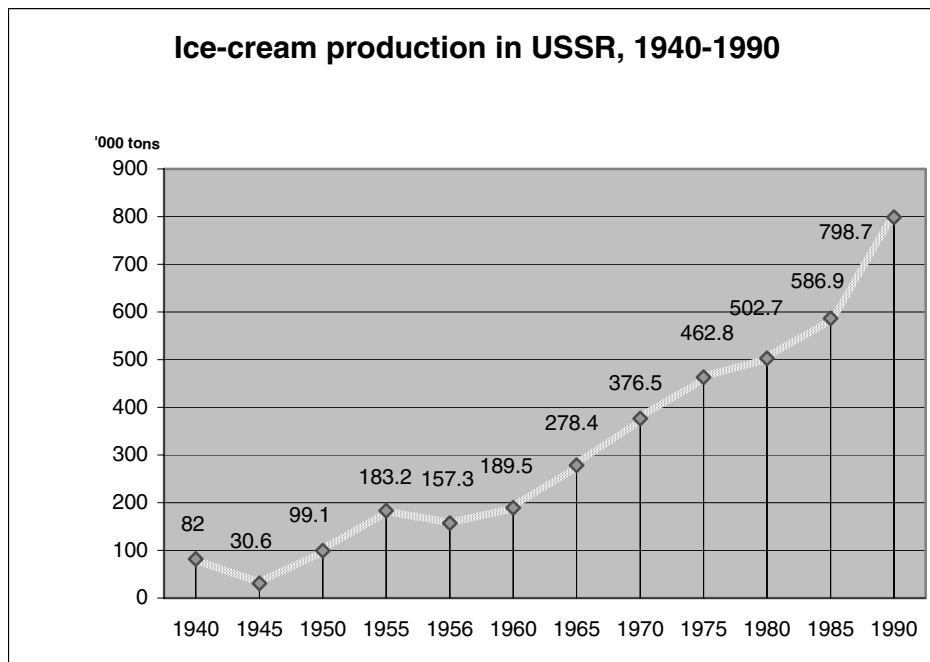
Source: Compiled from Ice-Fili documents and Goskomstat data.

^a By May 1998, half of ice cream companies changed to 10% VAT, which led to significant increase of production volumes.

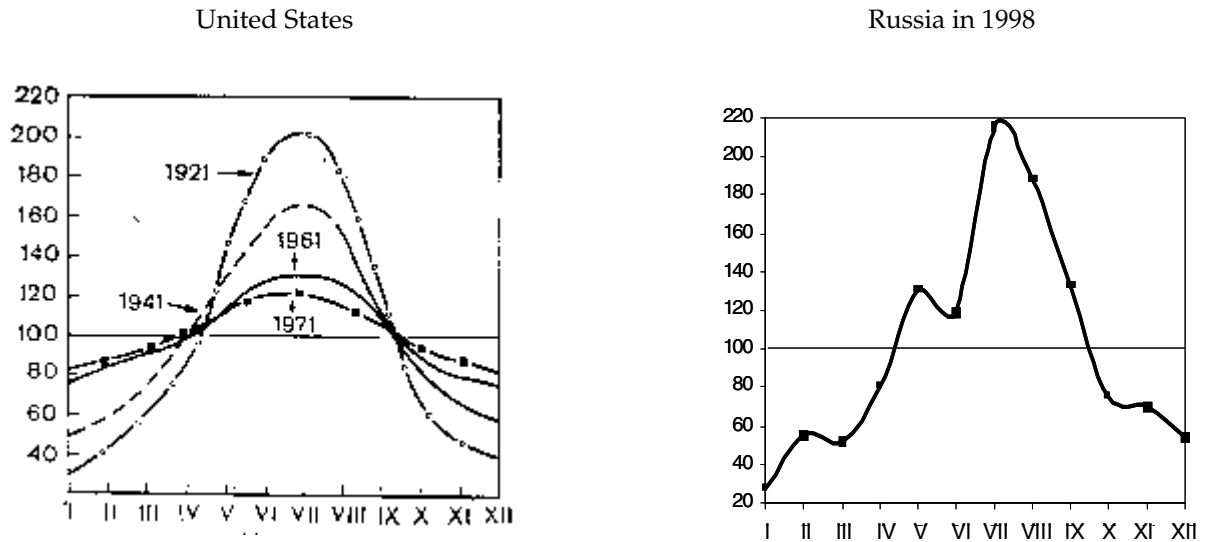
Exhibit 1c Production of Ice Cream by Ice-Fili

	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
Production volume (thousands of tons)	12	16	14	15	15	26	27.5	22	20	19
Market share (%)	N.A.	N.A.	N.A.	N.A.	6.8	10.3	8.5	6.0	5.7	5.2

Source: Company documents.

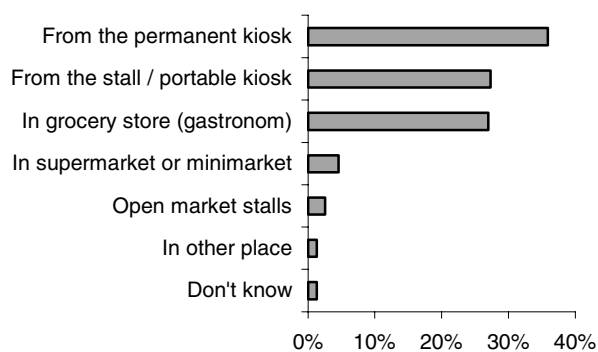
Exhibit 2 Ice Cream Production in USSR, 1940–1990

Source: Company documents.

Exhibit 3 Seasonality of Ice Cream Consumption Comparison

Seasonal index (average 100) – vertical axis
Months – horizontal axis

Source: www.d2d.ru, March 3, 2002.

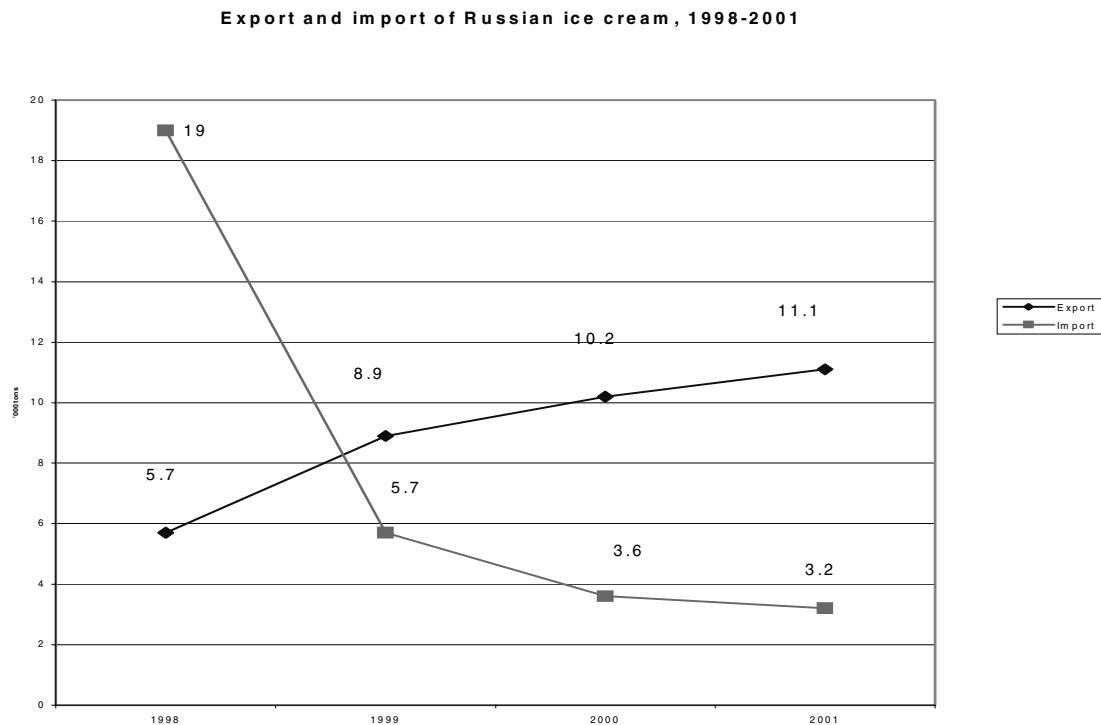
Exhibit 4 Where Most Frequent Purchases of Ice Cream Occur

Source: Adapted from "Ice cream: How to find a buyer," *Ice Cream and Frozen Foods Magazine*, Volume 1, 2001.

Exhibit 5 Standards for Ice Cream Production

Type of ice cream	Plombir	Cream	Milk	Sorbet
Minimum content of fat, %	12–15	8–10	2.8–3.5	0
Minimum content of sugar, %	14–16	12–14	15–16	27
Total content of dry products, %	38–39	32	29	30

Source: Company documents.

Exhibit 6 Imports and Exports of Russian Ice Cream, 1998–2001

Source: Adapted from "Production and realization of ice-cream and frozen foods," *Ice Cream and Frozen Foods Magazine*, Issue 2, 2002.

Exhibit 7a Ice-Fili Financial Statement (in thousands of U.S. dollars)

For the end of the year	2001	2000	1999	1998	1997	1996
<u><i>Assets</i></u>						
Cash	107	197	248	466	1,324	1,752
Accounts receivable	2,211	2,055	620	3,570	2,275	1,281
Cash reserves and Inventory	3,801	3,971	6,521	6,896	11,372	8,375
Other working capital	219	150	423	679	1,801	537
Total working capital	6,338	6,373	7,812	11,611	16,772	11,945
Intangible assets	1	8	11	10	5	4
PP&E	4,069	2,757	3,458	6,001	9,512	10,265
Other assets	1,424	1,468	1,364	728	571	2,519
Total assets	11,832	10,606	12,645	18,350	26,860	24,733
<u><i>Liabilities & Equity</i></u>						
Accounts payable	1,161	1,124	2,642	3,016	2,945	1,953
Short-term debt	29	31	-	-	-	-
Other current liabilities	4	0.2	1	2,064	3,735	2,784
Total current liabilities	1,194	1,155	2,643	5,080	6,680	4,737
Long-term liabilities	-	-	-	-	-	-
Equity	10,638	9,451	10,002	13,270	20,180	19,996
Total equity and liabilities	11,832	10,606	12,645	18,350	26,860	24,733
<u><i>Income Statement</i></u>						
Sales	25,147	27,206	32,672	35,988	68,892	34,083
Cost of goods sold	19,512	24,004	28,798	31,307	56,497	20,302
Gross profit	5,635	2,139	2,903	3,253	9,175	10,006
Income before taxes	1,951	2,121	2,816	3,809	8,612	10,259
Income tax	249	394	727	1,067	2,756	3,506
Net income	1,702	1,727	2,090	2,742	5,856	6,753
Return on assets	14.4%	16.3%	16.5%	14.9%	21.8%	27.3%
Return on equity	16.0%	18.3%	20.9%	20.7%	29.0%	33.8%

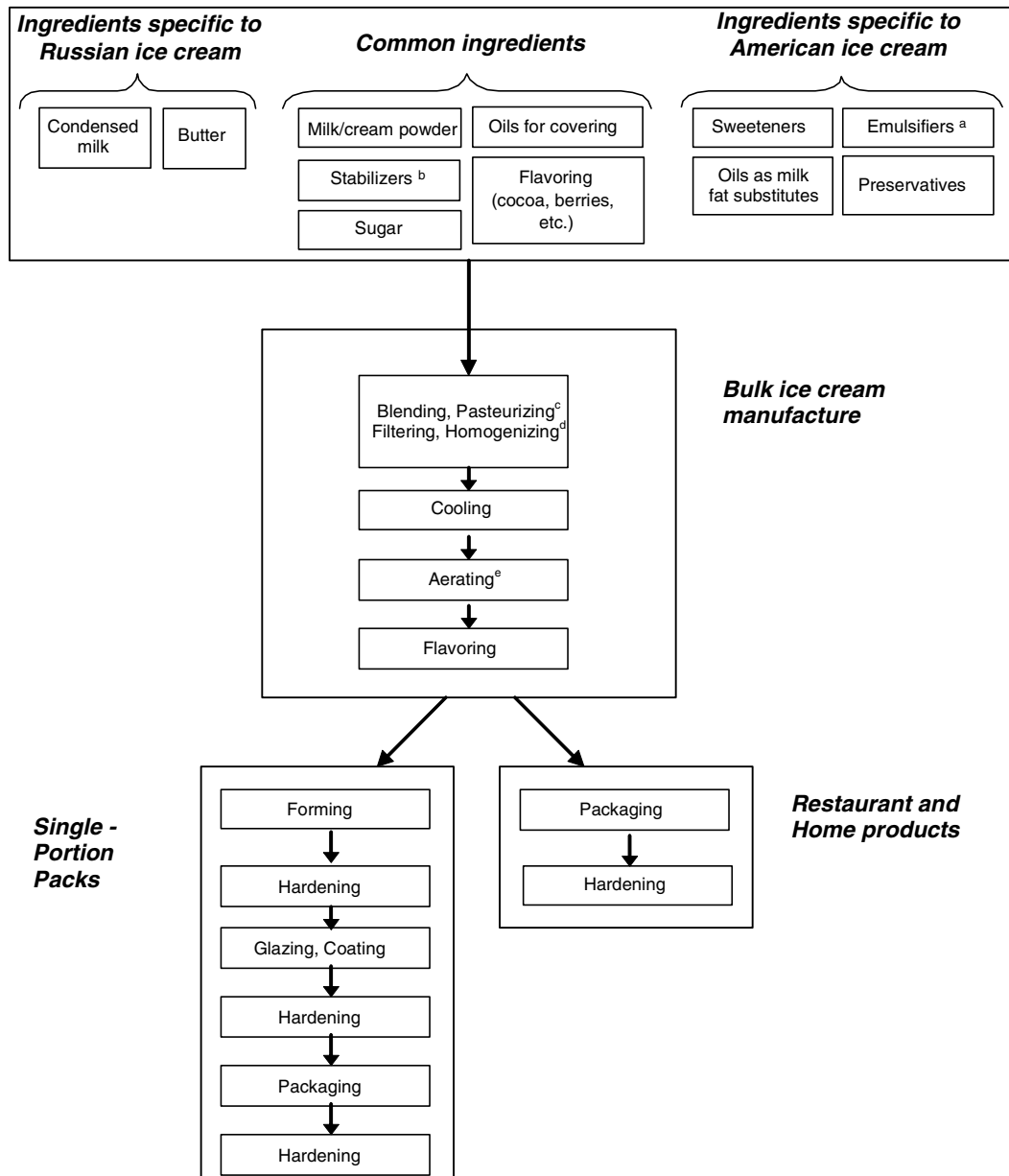
Source: Company documents.

Exhibit 7b Ice-Fili Financial Statement (in thousands of Russian rubles)

For the end of the year	2001	2000	1999	1998	1997	1996
<u>Assets</u>						
Cash	3,114	5,447	5,902	6,200	7,680	8,936
Accounts receivable	64,584	56,713	14,767	47,483	13,196	6,533
Cash reserves and inventory	110,989	109,609	155,195	91,716	65,955	42,711
Other working capital	6,392	4,138	10,064	9,032	10,446	2,737
Total working capital	185,079	175,907	185,928	154,431	97,277	60,917
Intangible assets	37	221	267	135	32	20
PP&E	118,823	76,080	82,295	79,814	55,168	52,352
Other assets	41,571	40,512	32,473	9,677	3,309	12,847
Total assets	345,510	292,720	300,963	244,057	155,786	126,136
<u>Liabilities & Equity</u>						
Accounts payable	33,908	31,024	62,889	40,116	17,083	9,960
Short-term debt	857	857	-	-	-	-
Other current liabilities	106	7	32	27,448	21,663	14,198
Total current liabilities	34,871	31,888	62,921	67,564	38,746	24,158
Long-term liabilities	-	-	-	-	-	-
Equity	310,639	260,832	238,042	176,493	117,040	101,978
Total equity and liabilities	345,510	292,720	300,963	244,057	155,786	126,136
<u>Income Statement</u>						
Sales	734,289	750,901	777,593	478,641	399,577	173,826
Cost of goods sold	569,736	662,513	685,385	416,388	327,684	103,542
Gross profit	164,553	59,029	69,097	43,269	53,216	51,029
Income before taxes	56,973	58,535	67,034	50,657	49,948	52,319
Income tax	7,268	10,882	17,294	14,192	15,985	17,883
Net income	49,705	47,653	49,740	36,465	33,964	34,436
Return on assets	14.4%	16.3%	16.5%	14.9%	21.8%	27.3%
Return on equity	16.0%	18.3%	20.9%	20.7%	29.0%	33.8%
Average exchange rate (Rubles for 1 U.S. dollar)	29.2	27.6	23.8	13.3	5.8	5.1

Source: Company documents.

Exhibit 8 Simplified Ice Cream Production Process



Source: Compiled from interviews and www.idf.org.

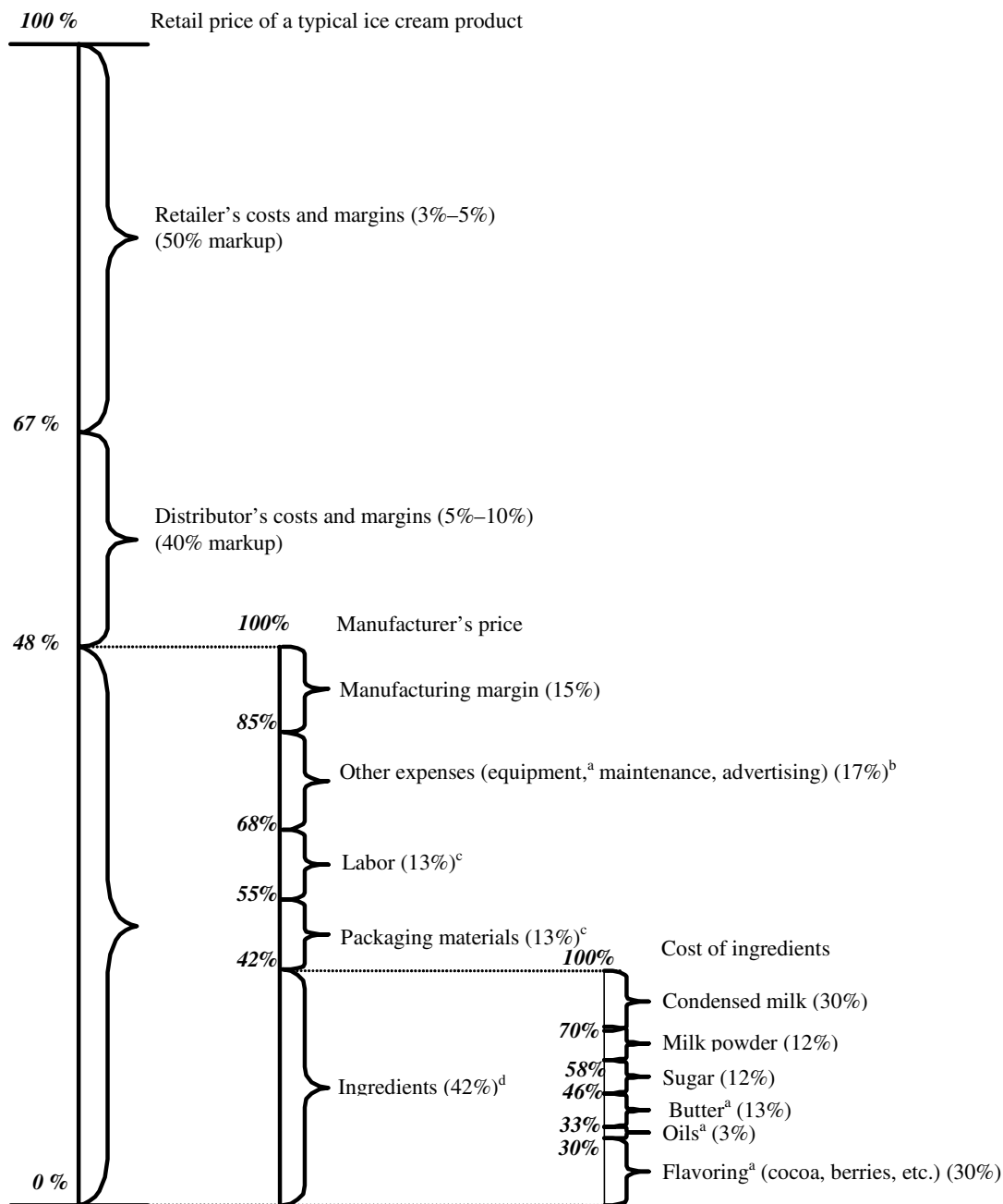
^a Emulsifiers such as lecithin and mono and diglycerides provide uniform whipping qualities to the ice cream during freezing, as well as providing a smoother, drier body and texture to the frozen form.

^b Stabilizers such as plant derivatives are used in small amounts to prevent the formation of ice crystals and to make the ice cream smoother.

^c Pasteurization refers to the process of heating a beverage or other food, such as milk or beer, to a specific temperature for a specific period of time in order to kill microorganisms that could cause disease, spoilage, or undesired fermentation.

^d Homogenization refers to the process that makes milk uniform in consistency by emulsifying the fat content.

^e Air is pumped in (about 50%) to make the product lighter.

Exhibit 9 Cost Structure for Ice Cream Delivered in Moscow (exclusive of VAT)

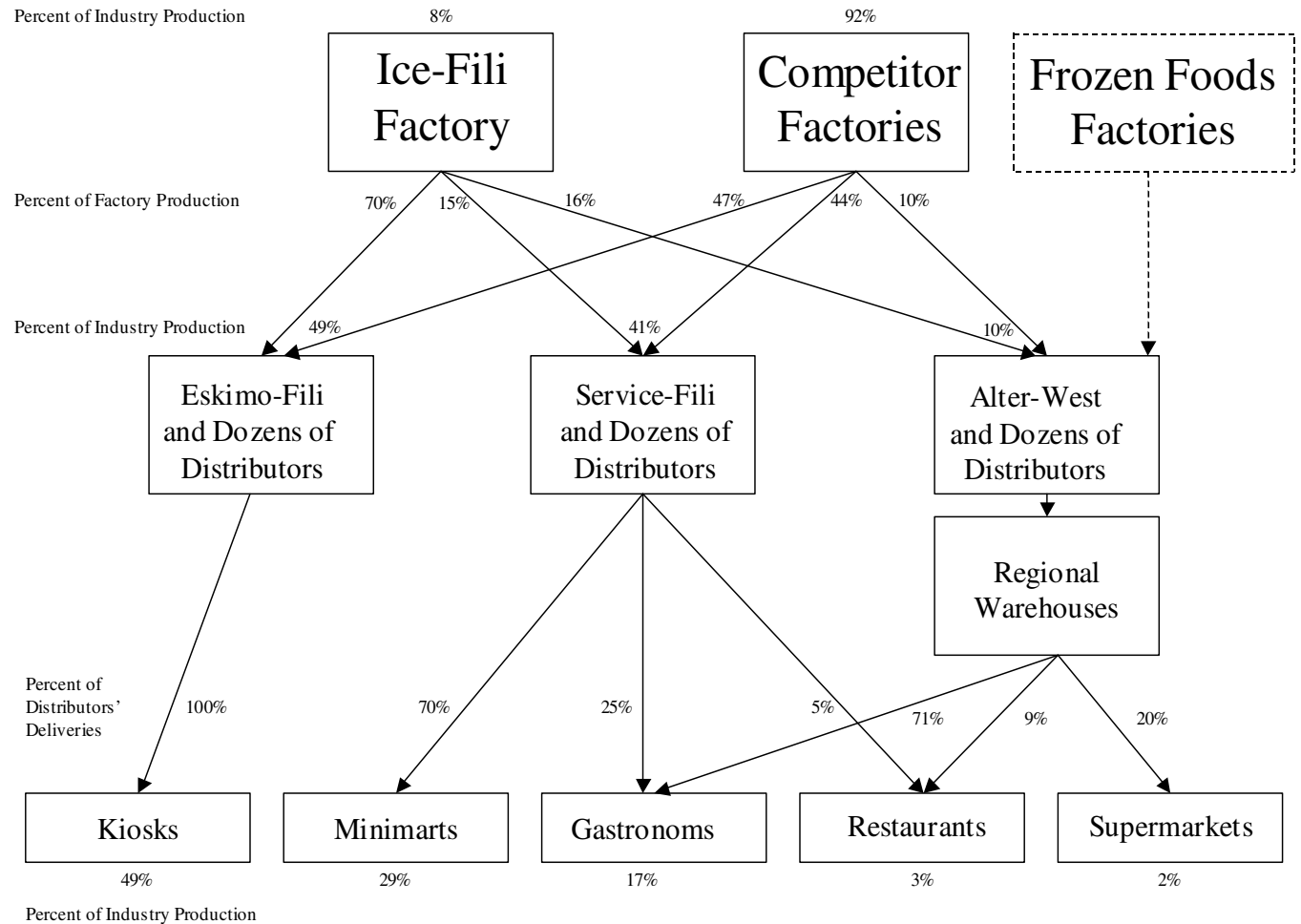
Source: Casewriter estimates.

^a These expenses may be subject to import duties.

^b Approximately 60% production-related expenses (80% were line-specific expenses, 20% were plant overhead).

^c Approximately 90% production-related expenses (80% were line-specific expenses, 20% were plant overhead).

^d Dairy fat substitutes could provide up to a 50% savings.

Exhibit 10 Representative Ice Cream Distribution Channels

Source: Casewriter estimates based on interviews.

Exhibit 11 Selected Competitors in Russian Ice Cream Market

Company	Location	Daily Production Capacity	Number of Factories	Date of Establishment	Largest Brand Names	Number of Ice Cream Products	Vertical Integration (beyond production)	Non-Ice Cream Products
Ice-Fili	Moscow	200 tons	1	1937	Likomka, Batonchik Fili	170	Distribution Some local retail	Dairy products such as margarine and mayonnaise
Service Holod	Moscow	70 tons	1	1950	N.A.	100	Distribution Retail	Wholesaler of wide range of food products
Baskin-Robbins	Moscow region	62 tons	1	1988, 1996 (production)	N.A.	30	Distribution Franchised local retail	None
Metelitsa	Moscow region	50 tons	1	1995	Ice cream cakes Venetsia, Metelitsa, Volshebnyi stakanchik	50	Distribution	None
Nestlé	Moscow region & Krasnoyarskiy Kray	45 tons	2	1997 (local production)	48 kopeek	25	Distribution	Coffee, chocolate, confectionary, pet food, bottled water, cereal
Alter-West	Moscow region	N.A.	1	1998 (production)	Ice cream cakes "I love you," "Silver rain"	80	Distribution	Frozen berries, mushrooms
Kolomenskii Khladokombinat	Moscow region	N.A.	1	N.A.	Alenka	N.A.	None	N.A.
Petroholod	St. Petersburg	50 tons	1	1939, 1946 (production)	Piterskoe	80	Distribution Local retail	Storage and wholesale trade of food products
Lipetskiy Hladokombinat	Lipetsk	100 tons	1	1962, 1980 (production)	Lipetskoe	100 (1 brand)	Local cafés and retail	Fish freezing
Inmarko	Novosibirsk, Omsk	90 tons	2 + 2 contracts for manufacturing	1992, 1996 (production)	Sibiryak, Keshka, Magnat, Fishka	80 (15 brands)	Distribution	None
Russkii Holod	Barnaul	65 tons	1 + contract manufacturing + 1 planned in Moscow in 2002	1987	Zabava	120	Distribution Retail	N.A.
Fabrika morozhenogo	Vladivostok	N.A.	1	1988	N.A.	30	None	N.A.
Yalga Holod	Saransk	N.A.	1	1963	Morozko	10 to 15	Distribution	N.A.
Belyi Medved	Vladimir	N.A.	1	1993	N.A.	10 to 20	None	None
Kaluzhskiy Hladokombinat	Kaluga	N.A.	1	1953	Darina, Vostorg, Gulliver	50 (10 brands)	Distribution	Wholesaler of wide range of food products

Source: Company Web sites.

Exhibit 12 A Small Sample of the 170 Ice-Fili Products



Source: Company.

Exhibit 13 Nestlé Brands in Russia



Source: www.Nestlé.ru.

Endnotes

- ¹ Haagen-Dazs was acquired by Pillsbury Company in 1983 and later became part of General Mills.
- ² "Russian ices have imports licked, say producers," *The Birmingham Post*, May 10, 1997.
- ³ Ibid.
- ⁴ *The Russia Journal*, September 7–3, 2001.
- ⁵ Ibid.
- ⁶ *The Economist*, October 6, 2001.
- ⁷ Casewriters' interview with A.G. Kladiy, May 27, 2002.
- ⁸ *Izvestiia*, July 18, 2001.
- ⁹ *Vedomosti*, March 12, 2002.
- ¹⁰ *Izvestiia*, July 18, 2001.
- ¹¹ *The Russia Journal*, No. 8, March 6, 2000.
- ¹² *Vedomosti*, September 5, 2001.
- ¹³ BBC Monitoring, October 28, 2000; *Moskovskie Novosti*, July 31, 2003.
- ¹⁴ HBS No. 594-059, "Food Distribution in Russia: The Harris Group and the LUX Store" (Boston: Harvard Business School Publishing, 1994).
- ¹⁵ www.2d2.ru.
- ¹⁶ HBS No. 594-059, "Food Distribution in Russia: The Harris Group and the LUX Store."
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- ¹⁸ Ibid.
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