

## ***Russian Ripples Hit U.S. Firms --- Sharp Slowdown in Consumer Spending Is Felt From Cigarettes to Copiers***

By Anjali Cordeiro

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The Russian economy has turned into a soft spot for U.S. consumer manufacturers and multinationals, a contrast with other major developing markets that have helped shore up the results of these companies during the global economic downturn.

Between January and June, Russia's economy contracted around 10% from a year earlier amid falling commodity prices and tight credit conditions. The effects of that contraction have trickled down to U.S. companies, which in recent years have sought to cash in on a boom in consumer spending in the region.

Companies including toothpaste maker Colgate-Palmolive Co. and cigarette seller Philip Morris International Inc. have in their recent quarters felt the effects of Russian consumers cutting back. Philip Morris saw shipments of its flagship highend Marlboro brand slip 19% in Russia as more smokers traded down to cheaper cigarettes. Colgate saw second-quarter sales fall 4.5% in its Greater Asia and Africa operations as volume gains in India and China failed to offset declines in such markets as Russia and Ukraine. These companies don't disclose profit numbers for Russia.

Consumer companies aren't the only ones feeling the pressure. Xerox Corp. said its second-quarter sales were hurt in part by weakness in its Russia operations as tight credit conditions weighed on business spending there.

Most multinationals don't publicly disclose sales from Russia and the region accounts for just one slice of their international earnings. But in recent years, the fast-growing market has become increasingly important owing to strong consumer spending.

"The pressure to buy is there and there is a lot of money sloshing around. It's an important market," says Marvin Zonis, a professor at the University of Chicago Booth School of Business.

As the U.S. plunged into recession, some of the largest American companies have relied on international growth to shore up their profits, but not all developing markets have held up equally. The contraction in the Russian economy is at odds with what consumer multinationals are seeing in the key Asian developing markets, with the Indian and Chinese economies still on track to grow this year, though at a slower pace.

Still, U.S. companies continue to push investment dollars toward Russia in the hopes of a longer-term payoff.

In July, PepsiCo Inc. along with a bottler announced plans to invest \$1 billion over three years in Russia to expand its snacks and beverages business. The company takes a "long-term view" of its investments, said spokesman Dick Detwiler. As in the U.S., the company has made a push to offer Russian consumers more affordable products -- like smaller snack packs that sell at prices beginning at eight rubles, or about 25 cents.

"The Russian economy is a proxy on the price of oil and gas. The fate of the consumer market in Russia is dependent on the price of oil and gas," says Prof. Zonis. By contrast, he points out that countries like India and China have far more diversified economies.

As the global economy improves and as demand for commodities picks up, the Russian economy is expected to pick up steam as well. Colgate said last month that macroeconomic conditions in the region are improving. Manufacturing and other data have pointed to potential improvements later in the year.

Still, this year is expected to be tough and the International Monetary Fund sees the Russian economy shrinking 6.5% in 2009.

"The crisis is not over in Russia yet," said Philip Morris International Chief Financial Officer Hermann Waldemer on a recent conference call with investors, pointing to high levels of unemployment. Russia, which has a large smoking population, is an important market for the cigarette giant.

A Philip Morris spokesman said via email that the company continues to invest in improving its products and business there. The company's cheaper cigarette brands like Bond Street and Optima saw sharp volume growth of 35% and 23%, respectively, in the second quarter in Russia, helping offset declines in higher price brands like Marlboro.

Global food giant Kraft Foods Inc., which in recent years has named Russia a "priority" international market, acknowledges that weaker consumer spending has hurt that market. But the food maker says it is still expanding market share and sales, and is on schedule to open a new biscuit manufacturing facility in Russia this October.

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