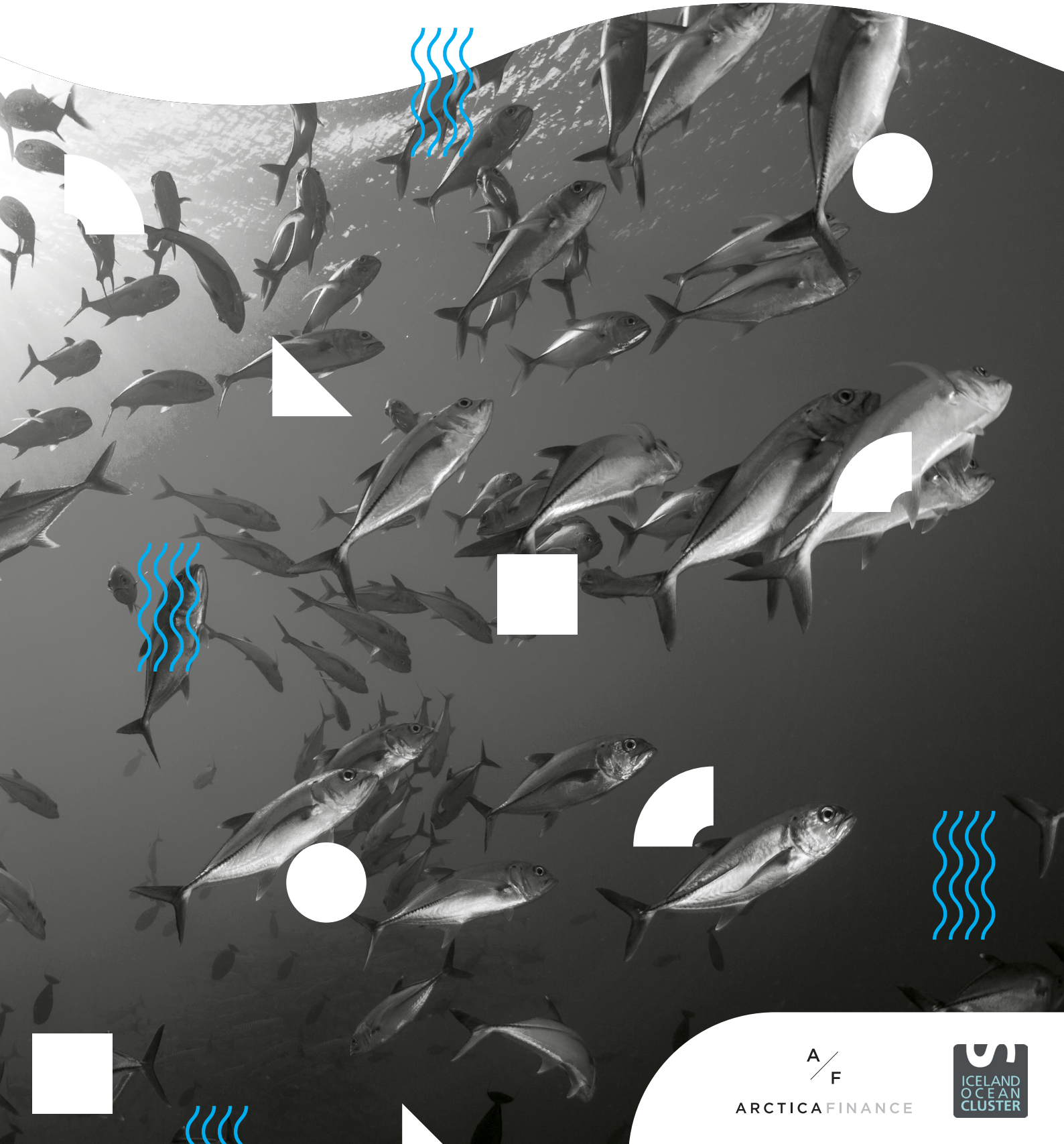
100% FISH

The Russian Seafood Modernization

A Message from Russia



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ICELAND OCEAN CLUSTER

Summary

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Fishery technology in Russia has long lagged behind that of other competing nations, especially in the North Atlantic. After years of technological divergence, however, the tide now seems to be turning in Russia. The country, which has the fourth longest coastline in the world, recently put an ambitious strategy in place to modernize its seafood sector, allocating massive resources to all areas of the industry, from infrastructure to fish processing. An investment quota mechanism was also established. This has created large opportunities for companies involved in fishery technology. Russia's grand plan for its fishing industry signals to other seafood nations that the future of fishing lies in technology and that if a large nation can revitalize its fishing industry, then others can too.

Strategic Plans

In 2009, the Russian government introduced a strategic plan for the reformation of its fishing industry, titled "Strategy for the Development of the Russian Federation Fisheries Complex for the Period until 2020." Its purpose was to create conditions for sustainable socioeconomic development of the Russian Federation's fishing industry and establish Russia as a leading fishing nation by 2020. This was to be achieved by transforming the fishing industry from being centered on raw material exports to being driven by innovation and a more consistent development of the value chain, as well as using biological resources in a sustainable manner. By doing so, the Russian fishing industry could boost its global competitiveness (Garant, 2009). The main objectives of the strategy were:

- Sustainability of fishery stocks, restoring them and developing aquaculture.
- Modernize the technology stage in fish processing and fishing fleet in domestic shipyards.
- Develop fishery science and technology and train qualified personnel in the fishing industry.
- Develop effective infrastructure in the domestic market for fish products.
- Develop the maritime infrastructure for services for the fishing fleet.
- Improve effectiveness of government fishery management, creating a competitive regulatory and institutional environment, encouraging business activity and increasing investments in the fishing industry.
- International cooperation and strengthening the position of Russian fishery products by developing increased value-added products.

An internal evaluation of the strategy's progress in 2015 revealed that only 26% of the fishing fleet had been renewed, where the aim was to build 380 fishing vessels and 120 refrigeration vessels before 2020. The strategy was aggressively revised and pushed further into the future, with a new deadline of 2030 (Radchenko, 2017).

The strategy was revised with the purpose of ensuring food security in the Russian Federation, in part due to public health considerations in ensuring a balanced diet. It was also revised to strengthen the country's economy, sustain an increased

contribution of the fishing industry to Russian gross domestic product (GDP), strengthen Russia's position in the global seafood market, increase employment and minimize negative environmental externalities (Federal Fishery Agency, 2017).

The main objectives following the revision were:

- Ensure national food security through an increase of fish per capita and consumption of fish products up to 22-27 kilograms per person a year, also making domestic seafood consumption 80-90% self-sufficient.

- Increase highly qualified job positions to 25,000 by 2030 and grow labor productivity by 150%.

- Increase aggregated fishing industry contribution to GDP by 5% per annum and increase gross profit of enterprises in the fishing sector by 200% per ton of catch.

- Strengthen the Russian Federation's leadership in world markets by reaching a 25% share of the European market in pollock and cod products and 10% of the Asia-Pacific market in pollock and salmon products.

- Develop and implement a national system of eco-labeling of fisheries and companies in the fishing industry.

- Consolidate legislation at the federal level on fishery catch marketing and pricing and economic relationships between the fishing companies and the government.

- Bring order and increased efficiency in port infrastructure, which are federally owned.

- Reduce the negative impact of fishing activities on the environment, confirmed by receiving an award from the Food and Agriculture Organization of the United Nations (FAO) by 2025.

The main target indicators of the strategy are increased aquaculture production, increased seafood production, increased technology in fish products, updated capacity of the fishing fleet, investments in the development of the fishing industry, and increased share of products with a high degree of processing (Federal Fishery Agency, 2017). The strategy thus emphasized modernizing the fishing sector, especially infrastructure, fish processing and fishing vessels.

One part of the plan focuses on refurbishing fishing terminals and increasing cold storage. Hundreds of millions of U.S. dollars are to be invested for that purpose with capital from the Russian state and private entities. Such projects have already begun, for example in the Kamchatka Peninsula in the Far East, with backing from Norebo, Russia's largest fishing company, and in Murmansk in northwestern Russia, with backing from private investors (SeafoodSource 2018a; SeafoodSource, 2018b).

The primary aim of the renovation efforts is to bring more Russian fishing vessels belonging to Russian companies to Russian ports by providing better fishing terminals, including cold storage facilities and services ranging from repair and maintenance to fuel. The main drawback, however, is that an increasing majority of medium to large fishing vessels in the Russian Far East go to countries like South Korea, China and Japan for services, where higher prices for services are justified with higher quality work at a much faster work rate. Better conditions in fishing terminals would in turn increase landed catch in Russia. This would also have the effect of increasing domestic fish supply and lowering the end price of fish for Russian consumers (SeafoodSource 2018a; SeafoodSource, 2018b).

While Russia's strategy might very well place the country at the forefront of the global seafood industry, there is still a lot of work to be done. This is especially due to the fact that exporting fish and landing abroad is still more profitable than domestic landings (SeafoodSource, 2018a). As Ilya Shestakov, head of the Russian Fisheries Agency has remarked, wild caught white fish can become a premium product, with higher price category and added value (FiskerForum, 2017).

Current Status of the Fishing Fleet and Processing Facilities

The Russian fishing fleet is old and fish processing techniques in Russia are, for the most part, worn-out and outdated. Most of the two thousand Russian fishing vessels are over 25 years old, manufactured in the 1970s and 80s, with an average age of around 30 years. The ships that have been scrapped over the last few years have not all been replaced, while the ones that have were mostly built in foreign shipyards. According to the Russian fishing strategy, half of the fleet is to be renewed over the next dozen years (SeafoodSource, 2018c; Flanders, 2017). However, the Russian plan is hampered by an outmoded fleet and substandard fish processing techniques. This limits the production capacity of the Russian fishing industry.

Investment Quota

As a result of the strategy for the Russian fishing industry, the Russian authorities established an investment quota mechanism. Legislation for creating a quota system in Russia was introduced in 2003, according to which quota was allocated for five years, from 2004 to 2008, based on historical catches. In 2009, the quota was allocated again, but for 10 years, from 2009 to 2018. Then, in 2016, quota was allocated for a 15-year period, from 2019 until 2033 (Radchenko, 2017).

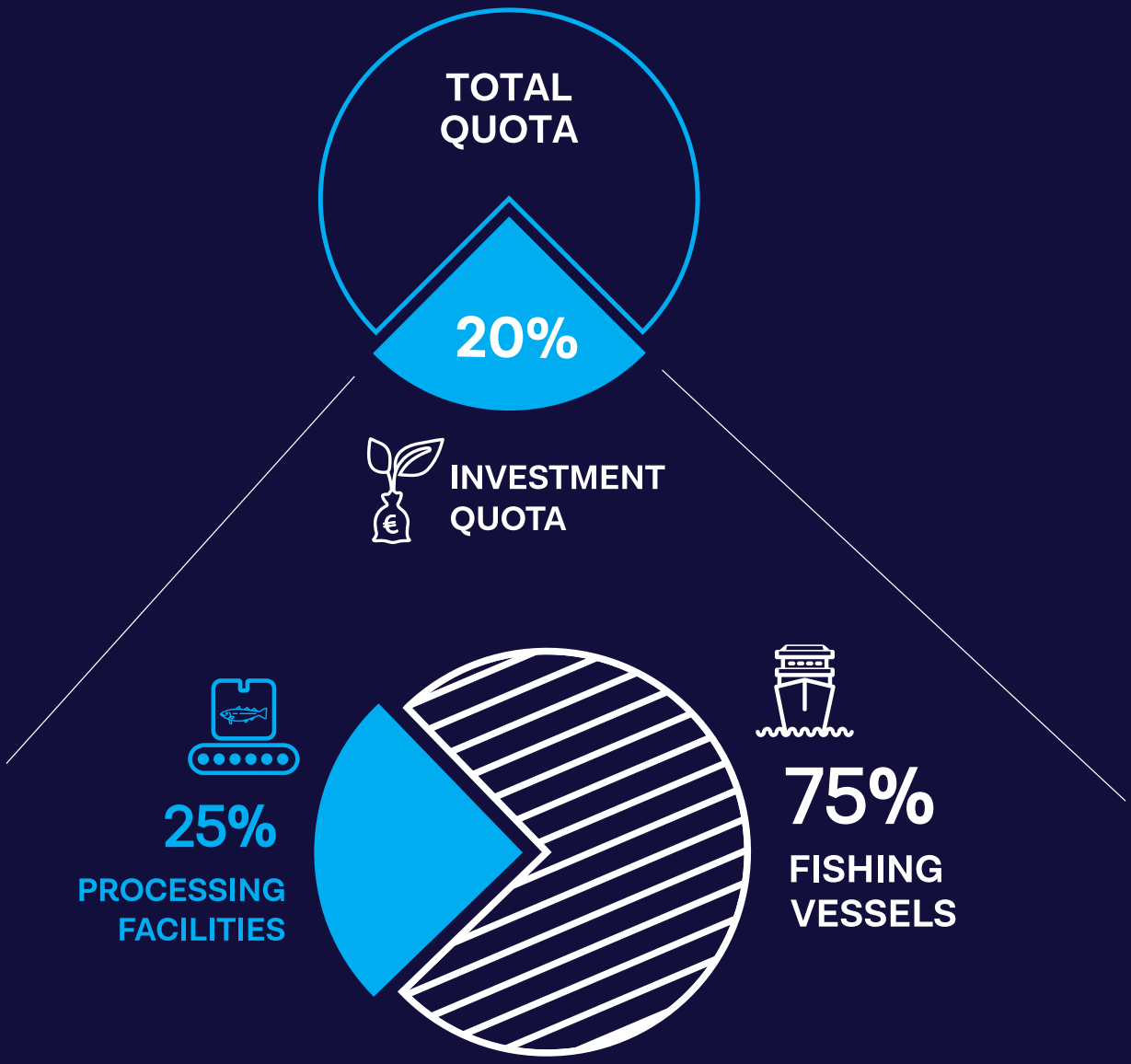
The initial results of the investment mechanism were published in March 2018. How the investment quota works is that a 20% share of the quota to be allocated in 2019 is put aside and subjected to allocation over 15 years based on planned investment in the fishing industry, as depicted in more detail below.

The mechanism aims at updating an old fishing vessel fleet and upgrading fish processing technology in Russia in exchange for an increase of quota for 15 years (Radchenko, 2017; SeafoodSource, 2018). The objective was to create a more economic and productive fishing industry. With the quota allocated for building ships, the investment quota arrangement stipulates that the ships be constructed in Russian shipyards. About 75% of the investment quota is allocated to investments in fishing vessels – mostly in fish processing – with the remainder being allocated to investments in processing facilities. Most of the quota is obtained by building fish processing vessels.

In 2018, application for the investment quota for larger ships (65 meters or longer), usually used for catching whitefish species like cod and Alaska pollock, ended. The allocation for fish processing facilities was also completed. Extra investment quota additions were made for crab, salmon and flatfish species. Although the official current number of ships to be built is not available, dozens of ships are being built as well as multiple processing facilities.

Then there are ships that are 25-65 meters in length, the so-called mosquito fleet. Originally, the renewal of these ships – around 150 to 200 in total – was to fall under the Investment quota mechanism. However, because the owners of the fleet are usually small companies with insufficient resources, they were instead provided with a 20% grant and 70% government-backed bank loans, with only a 10% equity requirement. These ships are mostly wet fish trawlers, which calls for land-based processing facilities. The idea is to structure their financing in a similar manner to the mosquito fleet to incentivize the construction of new processing plants.

The Investment Quota Mechanism



Continuing Opportunities in Russia

Russia's strategic plan for its fishing industry has some interesting side effects, such as increased demand for state-of-the-art technology in the fishing sector. Although opportunities for fishery technology companies seem to be running short, it may be argued that there are plenty of opportunities surrounding the mosquito fleet. When the investment quota is finished, perhaps only 20% of fish processing facilities that are needed will have been completed. With the fishing fleet, then, being only halfway on the strategic journey, there are perhaps perhaps ten years left of opportunities in Russia.

A point to note is that not every fishing company is using or can use the investment quota. These companies, however, face the choice of modernizing or else liquidating or becoming takeover targets of larger companies.The logic behind such a choice is simple. The smaller companies cannot compete with superior quality of fish and new ships – which are bigger, with better engines, more efficient and furbished with newest technology – can increase margins by up to 40% compared to ships that are 20 years old.

The effect of increased investment in the Russian fishing sector, combined with the quota system, might mirror how the Icelandic fishing sector has developed over the last decades. In Iceland, advancements in technology have been at the center of continuous consolidation in the fishing sector. This has created more opportunities for investment in fishery technology, as consolidation often stems from more efficient companies taking over less efficient ones and turning them into efficient companies.

A Message from Russia: A Broader View

Russia's undertaking in their fishing sector has a broader message for other seafood nations and the world as a whole.

First, there are ample opportunities in the global seafood sector for technological advancements, which are significant for the fishing industry. Consumers are demanding higher quality products and technological advancements can enhance efficiency and economization, as well as yield more value-added products.

Second, other seafood nations can draw lessons from and potentially model Russia's approach. It is important for other seafood nations to take notice of how a large seafood sector can be revitalized by following a strategic policy and ensuring commitment.

Third, it will be interesting to observe how the market will react to the higher quality products from Russia. These products will impact the global seafood market directly or indirectly. Russia can yield higher prices for better products, which might open new markets and increase demand for high quality seafood products.

Fourth, homogenous seafood product quality across nations can create opportunities for collaboration in sales and marketing. This is an important topic which will be covered in another article, which will examine the implications of the fishing revolution in Russia on this issue.

These lessons from Russia could prove useful to other seafood nations and provide an interesting narrative in the evolution of the global seafood sector.

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Thanks

The authors would like to express their gratitude and thanks to Knarr, Marel, Skaginn3x, Valka and Iceland Seafood for their valuable input and help. Special thanks to Haraldur Árnason, Sigurður Ólason, Kristmann Kristmannsson, Jón Birgir Gunnarsson, Helgi Hjálmarsson, Ágúst Sigurðarson, Teitur Gylfason and Vladimir Radchenko.

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