Cement industry in the Eurasian Economic Union
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The cement industry is one of the most dynamic industries in the Eurasian Economic Union (EAEU). In 2014, cement consumption in Russia reached a new record high. However, the introduction of economic sanctions against Russia has had adverse effects, likely to have resulted in a decline in domestic cement consumption in 2015. Analysts expect demand to grow by 2020 as Russia, Kazakhstan, Belarus, Kyrgyzstan and Armenia continue to upgrade infrastructure and pursue programs to support the industry.

The economic sanctions have brought about a number of serious challenges for the industry, including higher debt costs. This trend worries cement industry executives just as much as increases in energy prices have always done.

Funding constraints and lower cement consumption in 2015 intensified competition for consumer markets among industry players. Many companies are focused on resetting their cost base, boosting production efficiency and upgrading plants. More than 70% of respondents in our survey believe that these measures are crucial for the industry’s near-term growth. Most industry players (80% of respondents) also expect the closure of inefficient plants in the current economic environment, as well as more acquisitions by local producers that will lead to the consolidation of the market.

To succeed in their efforts to cut costs and gain a competitive edge in both the short and long term, it is essential for manufacturers to leverage best international practices. Our report includes a section dedicated to best available techniques (BAT) to help companies stay abreast of industry trends. We hope that the report will give you valuable insights for business growth.

We have surveyed cement manufacturers in Russia, Kazakhstan and Belarus for a third consecutive year. Our report, based on our findings, outlines key trends and challenges facing the industry. We would like to thank all survey participants for sharing their thoughts with us.
The cement industry in Russia, Belarus, Kazakhstan, Armenia and Kyrgyzstan in 2014-15
The cement industry in Russia

Cement production and consumption in Russia slowed in 2014, by 3.0% and 2.7% year-on-year, respectively.

The extra demand was primarily satisfied by increased domestic production in 2014. However, in the first seven months of 2015, cement production and consumption declined by 9.3% and 11.6% year-on-year, respectively. Analysts from RD Construction attributed the downward trend to lower domestic demand, as well as reduced imports and exports in the current period of economic downturn in Russia.1

The share of imports in total domestic consumption dropped from 7.2% in 2013 to 6.7% in 2014. Turkish2 and Lithuanian imports fell in 2014 under the pressure of the economic sanctions and Russia's sluggish economic growth.3 Cement imports from Kazakhstan soared by 130% in 2014 as the country's industry saw the arrival of new players and the construction of new plants, but they plummeted by 40.8% year-on-year in the first seven months of 2015 amid the weakening of the Russian rouble.

The share of exports in total domestic production was stable, at 2.6% in 2014 and 2.8% in the first seven months of 2015, with nearly all exports in 2014 (over 98.5%) delivered to Kazakhstan, Belarus and Azerbaijan. Exports to Kazakhstan and Azerbaijan dropped in 2014 as newly launched plants in those countries strengthened the capacity of the local industries.4

Table 1. Russian cement imports by country of origin (thousands of tonnes)

<table>
<thead>
<tr>
<th>Country</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
</tr>
</thead>
<tbody>
<tr>
<td>Belarus</td>
<td>388</td>
<td>981</td>
<td>1270</td>
<td>1590</td>
</tr>
<tr>
<td>Iran</td>
<td>77</td>
<td>462</td>
<td>720</td>
<td>660</td>
</tr>
<tr>
<td>Turkey</td>
<td>980</td>
<td>1874</td>
<td>1095</td>
<td>563</td>
</tr>
<tr>
<td>Sweden</td>
<td>130</td>
<td>175</td>
<td>367</td>
<td>462</td>
</tr>
<tr>
<td>Latvia</td>
<td>248</td>
<td>302</td>
<td>300</td>
<td>359</td>
</tr>
<tr>
<td>China</td>
<td>254</td>
<td>211</td>
<td>204</td>
<td>249</td>
</tr>
<tr>
<td>Kazakhstan</td>
<td>4</td>
<td>63</td>
<td>106</td>
<td>240</td>
</tr>
<tr>
<td>Lithuania</td>
<td>182</td>
<td>189</td>
<td>238</td>
<td>171</td>
</tr>
<tr>
<td>Poland</td>
<td>89</td>
<td>93</td>
<td>113</td>
<td>137</td>
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<tr>
<td>South Korea</td>
<td>127</td>
<td>123</td>
<td>127</td>
<td>135</td>
</tr>
<tr>
<td>Others</td>
<td>337</td>
<td>612</td>
<td>483</td>
<td>231</td>
</tr>
<tr>
<td>Total</td>
<td>2816</td>
<td>5085</td>
<td>5023</td>
<td>4797</td>
</tr>
</tbody>
</table>

Source: CM Pro Ltd. (CMPRO)

Table 2. Russian cement exports by destination country (thousands of tonnes)

<table>
<thead>
<tr>
<th>Country</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kazakhstan</td>
<td>648</td>
<td>840</td>
<td>1092</td>
<td>921</td>
</tr>
<tr>
<td>Belarus</td>
<td>153</td>
<td>276</td>
<td>414</td>
<td>543</td>
</tr>
<tr>
<td>Azerbaijan</td>
<td>362</td>
<td>289</td>
<td>262</td>
<td></td>
</tr>
<tr>
<td>Others</td>
<td>44</td>
<td>23</td>
<td>42</td>
<td>27</td>
</tr>
<tr>
<td>Total</td>
<td>1189</td>
<td>1501</td>
<td>1837</td>
<td>1753</td>
</tr>
</tbody>
</table>

Source: CMPRO

Table 3. Key indicators of the Russian cement market in 2005-14 and the first seven months of 2015

|------------------|------|------|------|------|------|------|------|------|------|------|              |                                |
| Output, thousands of tonnes | 48 534 | 54 731 | 59 933 | 53 548 | 44 266 | 50 371 | 55 936 | 61 516 | 66 419 | 68 437 | 48 907        | -9,3%                          |
| Imports, thousands of tonnes | 400 | 790 | 2757 | 8130 | 1300 | 1133 | 2816 | 5087 | 5023 | 4799 | 2291         | -40,8%                         |
| Exports, thousands of tonnes | 3100 | 3207 | 1869 | 804 | 1600 | 1748 | 1188 | 1501 | 1837 | 1752 | 1372         | -1,2%                          |
| Consumption, thousands of tonnes | 45 834 | 52 314 | 60 821 | 60 874 | 43 966 | 49 756 | 57 563 | 65 102 | 69 605 | 71 483 | 49 826        | -11,6%                         |
| Purchase price, RUB per tonne, incl. VAT and delivery charges | 3088 | 3577 | 4041 | 3906 | 3873 | n/a | n/a |      |      |      |      |                                |
| Market capacity, RUB b | 154 | 206 | 263 | 272 | 277 | n/a | n/a |      |      |      |      |                                |
| Imports, % of consumption | 1,5% | 4,5% | 13,4% | 3,0% | 2,3% | 4,9% | 7,8% | 7,2% | 6,7% | 4,6% |              |                                |
| Exports, % of output | 6,4% | 5,9% | 3,1% | 1,5% | 3,6% | 3,5% | 2,1% | 2,4% | 2,8% | 2,6% | 2,8% |              |                                |
| Increase in output, % | 12,8% | 9,5% | -10,7% | -17,3% | 13,8% | 11,0% | 10,0% | 8,0% | 3,0% |      |      |                                |
| Increase in consumption, % | 14,1% | 16,3% | 0,1% | -27,8% | 13,2% | 15,7% | 13,1% | 6,9% | 2,7% |      |      |                                |
| Increase in purchase price, RUB per tonne, incl. VAT and delivery charges, % | 15,8% | 13,0% | -3,3% | -0,9% |      |      |      |      |      |      |      |                                |

Source: CMPRO
The Russian cement industry comprises more than 10 major producers and a similar number of small local companies. The five largest industrial groups accounted for 63.3% of the market in 2014, marginally up from the previous year. The share of major cement manufacturing companies owned by international groups totaled 19.6% in 2014. Other industry participants were represented by local producers.

The market shares held by Russia’s major cement manufacturers in 2014 are shown in Figure 1.

While the key fundamentals of the Russian cement market may have worsened, demand is expected to rebound as the domestic construction industry needs to provide new homes and infrastructure, as well as implement a number of large-scale projects for the 2018 FIFA World Cup. Three stadiums (Spartak in Moscow, Fisht in Sochi and Kazan Arena in Kazan) have already been completed. Work is underway to build or reconstruct nine more arenas. Under the Order of the Russian Ministry of Sport No. 887 of 16 September 2015, a total of RUB 654b is to be spent on developing the required infrastructure.

The federal-level program, The Development of Russia’s Transport System, 2010–20, approved by Directive of the Russian Government No. 848 of 5 December 2001, outlines the following targets that must be achieved from 2015 through 2020:

- The construction of 14,800km of federal public roads in accordance with industry standards
- The commissioning of 342km of railway lines

The program budget is set at RUB 11,618.4b.

In the longer term, cement demand will be spurred by massive infrastructure projects, including:

- The construction of 11,200km of higher-speed and high-speed rail networks under the Russian Railways’ development strategy for the period until 2030
- The construction of a bridge across the Kerch Strait to provide an all-season link between the Crimean peninsula and Krasnodar Krai. This project requires RUB 218.5b of investment and is to be completed between 2015 and 2018
- The construction of a rail line bypassing Ukraine. This 2015–17 project requires RUB 56.6b in investment
- The construction of the 12,600km-long Astrakhan North Bypass, which will connect the northern and northwestern industrial areas of the Russian city and provide convenient access to the M6 highway. The project costs are estimated at RUB 23b. The construction period is 2014-20
- The reconstruction of the Gumrak airfield in Volgograd. The project costs are estimated at RUB 3b. The construction period is 2015-17

Per capita cement consumption in Russia jumped from 352kg in 2010 to 500kg in 2014, growing by 9% a year on average, while in China it increased from 1,100kg to 1,800kg in the period, an average 13% a year.

Figure 1. Major cement manufacturers’ share in total output in 2014 (%)

Source: CMPRO

Figure 2. New housing construction in Russia (actual data for 2014)

Sources: Rosstat, Amikron-Consulting LLC

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5 Vedomosti.ru.
According to CM Pro Ltd. (CMPRO) and EY experts, cement consumption in 2015 is likely to remain level with the previous year at 71 million tonnes. The Russian Ministry of Construction projects that domestic cement demand will rise to 97.8 million tonnes by 2020.\(^6\) However, major international players have a rather conservative outlook on the Russian market, expecting demand to grow by 3.1%-3.3% a year on average, to 86 million-87 million tonnes in the period until 2020.

A total of 81 million sq m of new housing was built in Russia in 2014, 14.9% more than a year earlier. The country’s housing stock totaled 23.7 sq m of dwelling space per person in 2014. Up to 90 million sq m of new homes were projected to be completed in 2015, mainly under government programs aimed at improving housing conditions for households.

According to government plans, in the period up to 2020, up to 140 million sq m of new homes will be completed.

The Russian Ministry of Construction unveiled a new residential building program called “Housing for the Russian Family” at a meeting of the Presidium of the Presidential Council on High-Priority National Projects and Demographic Policy held in mid-March 2014. Pursuant to amendments to a Directive of the Russian Government of 2 March 2015, the price ceiling on one square meter of economy-class housing was raised from RUB30,000 to RUB35,000 on 2 March 2015. The decision adjusted the price for projected inflation.\(^7\) Regional prices were set at even lower levels: within 80% of the market price for a square meter. The Government will fund the development of engineering infrastructure through long-term loans issued by the Agency for Housing Mortgage Lending. A total of 25 million sq m of new economy-class housing will be built, including 5 million sq m in 2015, 6 million sq m in 2016 and 14 million sq m in 2017.

Additional demand for cement is expected to be generated under the federal program Sustainable Rural Development in 2014-17 and in the period until 2020, approved by Directive of the Russian Government No. 598 of 15 July 2013. The program provides for the construction of 5.4 million sq m of new housing for rural residents, including 3 million sq m for young couples and young professionals. The program costs are estimated at RUB299b.

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6 cmpro.ru.

7 ahml.ru.

Geography shapes the Russian market

The Russian cement industry is characterized by an uneven distribution of plants. This is illustrated in Figure 3.

In 2014, Russia experienced shortages of domestically produced cement estimated at 3 million tonnes, largely owing to the insufficient development of reserves and rather low capacity-utilization rates. In particular, cement shortages hit the Central Federal District and the Northwestern Federal District while the Volga Federal District and the Siberian Federal District witnessed an oversupply. Cement consumption was down in the Southern Federal District after the completion of venues and infrastructure for the Winter Olympics in Sochi, leading to excess production.

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Figure 3. Cement production and consumption by federal district in 2010-14 (thousands of tonnes)

Sources: SMPRO, Rosstat
Kazakhstan’s annual cement production capacity totaled 14.2 million tonnes at the end of 2014. This figure is expected to reach 15.9 million tonnes after the completion of the second phase in the development of the cement industry.

The Program for the Development of the Construction and Building Materials Industries in Kazakhstan in 2010–20, pursued under two larger programs (GPIIR-1 and GPIIR-2), remains the key growth driver. GPIIR-2 will enable the country’s construction materials industry to satisfy no less than 80% of domestic demand.

Kazakh construction market prospects

Executives of Kazakh construction materials companies are expecting greater demand for their materials and tighter competition in the near term. In particular, they say, demand will be driven by preparations for the international exhibition EXPO-2017 in Astana, which will be dedicated to alternative energy sources. The required investment is estimated at KZT500b (US$3b). The project will occupy a total area of 173.4ha, with 25ha to be used by the exhibition facilities and the remaining 148ha intended for residential buildings, social infrastructure, education and health care facilities, shopping and entertainment centers, and parks.

8 ИА «Новости-Казахстан».

The market will get another boost from the State Program for the Development and Integration of Transport Infrastructure in Kazakhstan in the period until 2020, approved by a Presidential Decree of 13 January 2014. Total public and private investments in the program are estimated at KZT5.2 trillion (approximately US$33b). The program objectives include reconstructing and repairing roads and rail lines (30,000km and 8,000km, respectively), building civil aviation and water transport infrastructure, constructing terminals inside and outside the country, and improving roadside services. Around 200 infrastructure projects worth a total of US$28.6b are in the pipeline. In June 2014, the Kazakh Ministry of Transport and Communications announced plans to extend the program for another 10 years.

9 polsoz.fu-berlin.de.

Table 4. Key indicators of the Kazakh cement market in 2005–14

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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Output, thousands of tonnes</td>
<td>4181</td>
<td>4880</td>
<td>5699</td>
<td>5837</td>
<td>5694</td>
<td>6683</td>
<td>4181</td>
<td>6392</td>
<td>7107</td>
<td>8187</td>
</tr>
<tr>
<td>Imports, thousands of tonnes</td>
<td>1890</td>
<td>2631</td>
<td>3506</td>
<td>1826</td>
<td>782</td>
<td>1010</td>
<td>1890</td>
<td>1300</td>
<td>1550</td>
<td>1230</td>
</tr>
<tr>
<td>Exports, thousands of tonnes</td>
<td>4</td>
<td>1</td>
<td>–</td>
<td>131</td>
<td>25</td>
<td>199</td>
<td>4</td>
<td>180</td>
<td>205</td>
<td>415</td>
</tr>
<tr>
<td>Consumption, thousands of tonnes</td>
<td>6067</td>
<td>7510</td>
<td>9205</td>
<td>7532</td>
<td>6451</td>
<td>7494</td>
<td>6067</td>
<td>7512</td>
<td>8452</td>
<td>9002</td>
</tr>
<tr>
<td>Imports, % of consumption</td>
<td>31.2%</td>
<td>35.0%</td>
<td>38.1%</td>
<td>24.2%</td>
<td>12.1%</td>
<td>13.5%</td>
<td>31.2%</td>
<td>17.3%</td>
<td>18.3%</td>
<td>13.7%</td>
</tr>
<tr>
<td>Exports, % of output</td>
<td>0.1%</td>
<td>0.0%</td>
<td>0.0%</td>
<td>2.2%</td>
<td>0.4%</td>
<td>3.0%</td>
<td>0.1%</td>
<td>2.8%</td>
<td>2.9%</td>
<td>5.1%</td>
</tr>
<tr>
<td>Increase in output, %</td>
<td>16.7%</td>
<td>16.8%</td>
<td>2.4%</td>
<td>-2.4%</td>
<td>17.4%</td>
<td>-37.4%</td>
<td>52.9%</td>
<td>11.2%</td>
<td>15.2%</td>
<td></td>
</tr>
<tr>
<td>Increase in consumption, %</td>
<td>23.8%</td>
<td>22.6%</td>
<td>-18.2%</td>
<td>-14.4%</td>
<td>16.2%</td>
<td>-19.0%</td>
<td>23.8%</td>
<td>12.5%</td>
<td>6.5%</td>
<td></td>
</tr>
</tbody>
</table>

Source: CMPRO
A total of 7.5 million sq m of new housing was built in Kazakhstan in 2014, more than analysts expected. The country’s housing stock averaged out at 21 sq m of dwelling space per person.

Astana, the country’s largest city, ranks first in the amount of dwelling space per person (27.7 sq m in 2013). According to kn.kz, a website dedicated to real estate news and analysis, a total of 2.255 million sq m of new homes will be built in Astana annually until 2017.

The Government of the Republic of Kazakhstan, by its Directive No. 728 of 28 June 2014, approved the Program for Regional Development in the period until 2020, effective from 1 January 2015, to improve standards of living in the country, boost infrastructure development and spur economic growth across regions.

The following efforts should be undertaken to ensure program success:
- Promoting the territorial development of the country
- Creating comfortable conditions for citizens by driving improvements in areas such as environmental protection, housing construction, transportation and utilities
- Adopting a holistic approach for addressing housing construction challenges to make homes more affordable for people.

The program is to be implemented between 2015 and 2019 with no intermediary phases planned. A total of 38.1 million sq m of new housing will be built in the period.

Figure 4. New housing construction in Kazakhstan (actual data for 2014)

Sources: Affordable Housing 2020 Program, Agency of Statistics of the Republic of Kazakhstan
Cement industry in Belarus

The modernization project has increased the total production capacity of the Belarusian cement industry to 10.5 million tonnes. Domestic demand totaled 4.5 million tonnes in 2014.

In late 2008, Belarus embarked on a large-scale cement industry modernization project to build new capabilities in cooperation with Chinese state company CITIC Construction Co. The project was mainly funded by US$530 million in loans issued by the Export-Import Bank of China to cement manufacturers.

In 2013, the Belarusian Government decided that it would pay compensation to the cement manufacturers for interest on bank loans, totaling 50% of the National Bank’s refinancing rate on Belarusian-ruble loans and 50% of the contractual interest rates on loans denominated in foreign currency. However, in July 2014, the companies were fully exempted from any interest payments on such loans. On 1 June 2014, the Belarusian Government introduced the licensing requirement for cement importers in an attempt to provide stronger support for domestic manufacturers. The underlying licensing condition is that the contractual price of cement imports into Belarus should not be lower than the minimum price set under domestic supply contracts between cement manufacturers and the Belarusian Ministry of Architecture and Construction.

To boost domestic demand for cement, the Belarusian Council of Ministers made amendments to the technical code in July 2014, requiring road builders to use cement as the paving material.

In 2014, Belarus exported approximately 1.6 million tonnes of cement to Russia, or 91% of the country’s total cement exports. According to Belarusian Architecture and Construction Minister Anatoly Cherny, Belarus’s cement exports to Russia were projected to total 2 million tonnes in 2015.

In mid-2014, nine cement manufacturers, including OJSC Belarusian Cement Plant and OJSC Krichev-Cementshifer, were consolidated into one managing company of holding company Belarusian Cement Company, established to improve the performance of the domestic cement industry as production costs dropped. To make domestically produced cement more competitive, there are also plans to implement dry process technology at cement kilns that use a wet process. This program is to be completed before 2017. According to Cherny, Belarus was projected to produce 6.1 million tonnes of cement in 2015.

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10 belta.by.

Table 5. Key indicators of the Belarusian cement market in 2005-14

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</thead>
<tbody>
<tr>
<td>Output, thousands of tonnes</td>
<td>3131</td>
<td>3495</td>
<td>3821</td>
<td>4219</td>
<td>4350</td>
<td>4531</td>
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<tr>
<td>Imports, thousands of tonnes</td>
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<td>784</td>
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<tr>
<td>Exports, thousands of tonnes</td>
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<td>1389</td>
<td>1798</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>Consumption, thousands of tonnes</td>
<td>4393</td>
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<tr>
<td>Imports, % of consumption</td>
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<td>16.1%</td>
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<td>Exports, % of output</td>
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<tr>
<td>Increase in output, %</td>
<td>11.6%</td>
<td>9.3%</td>
<td>10.4%</td>
<td>3.1%</td>
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<td>6.4%</td>
<td>3.9%</td>
<td>10.2%</td>
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<tr>
<td>Increase in consumption, %</td>
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<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td>2.1%</td>
<td>1.3%</td>
<td></td>
</tr>
</tbody>
</table>

Source: National Statistical Committee of the Republic of Belarus
New housing construction

New housing construction in Belarus increased by 5% to 5.5 million sq m in 2014. A total of 46.9 million sq m of new homes were completed in Belarus in 2006-14, with more than 50% of them built with public funds. Belarus’s housing stock totaled 26.1 sq m of dwelling space per person in 2014.

One of the objectives of the Government’s housing policy is to increase the country’s housing stock to 27-28 sq m per person in 2015.

Under the housing construction program as amended on 30 June 2015, completions are to total 4 million sq m in 2015, which will include 3.5 million sq m of new homes for individuals on housing waiting lists (the construction of 2.8 million sq m is to be funded by the Government).11

While new housing construction rates are projected to drop in the near term, construction output will grow, fueled by a few massive projects:

➢ Work began in September 2015 to build a new district called Minsk Mir that will comprise residential buildings with a total area of 2 million sq m, a shopping and entertainment center and an international financial hub. The completion of the US$3.5 million project is scheduled for 2027.

➢ The construction of a new stadium in Minsk in the latter half of 2015. The new area was to open in September 2015. The project costs were estimated at EUR94 million.

In 2013, the authorities took measures to lower interest rates on loans provided for the construction of social housing and residential premises for commercial use.12 The refinancing rate of the National Bank of the Republic of Belarus decreased from 30% at the beginning of 2013 to 25%.

11 belta.by.


Figure 5. New housing construction in Belarus

Source: National Statistical Committee of the Republic of Belarus
Cement industry in Armenia

Cement production in Armenia dropped by 0.9% in 2014 from the previous year. This was due to lower demand from the domestic construction industry.13

The share of imports in total domestic consumption increased from 1.4% in 2013 to 2.1% in 2014. Nearly 98% of total domestic consumption was imported from Iran.14 Cement exports fell by 39.4% year-on-year in 2014 as Georgia, Armenia’s major importer, launched a cement plant in the Georgian city of Rustavi that helped satisfy some of its domestic demand.15

Armenia operates two major cement plants:

- CJSC Ararat Cement. The plant has an annual cement production capacity of 1.2 million tonnes and uses a dry process.
- CJSC Mika Cement. The plant has an annual cement production capacity of 1.2 million tonnes and uses a wet process.

Table 6. Key indicators of the Armenian cement market in 2010-14

<table>
<thead>
<tr>
<th></th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
</tr>
</thead>
<tbody>
<tr>
<td>Output, thousands of tonnes</td>
<td>488</td>
<td>422</td>
<td>438</td>
<td>431</td>
<td>427</td>
</tr>
<tr>
<td>Imports, thousands of tonnes</td>
<td>2</td>
<td>2</td>
<td>2</td>
<td>3</td>
<td>8</td>
</tr>
<tr>
<td>Exports, thousands of tonnes</td>
<td>38</td>
<td>98</td>
<td>136</td>
<td>185</td>
<td>73</td>
</tr>
<tr>
<td>Consumption, thousands of tonnes</td>
<td>452</td>
<td>326</td>
<td>304</td>
<td>249</td>
<td>362</td>
</tr>
<tr>
<td>Imports, % of consumption</td>
<td>0.3%</td>
<td>0.5%</td>
<td>0.6%</td>
<td>1.4%</td>
<td>2.1%</td>
</tr>
<tr>
<td>Exports, % of output</td>
<td>7.8%</td>
<td>23.2%</td>
<td>31.1%</td>
<td>43.0%</td>
<td>17.1%</td>
</tr>
<tr>
<td>Increase in output, %</td>
<td>-13.5%</td>
<td>3.8%</td>
<td>-1.6%</td>
<td>-0.9%</td>
<td></td>
</tr>
<tr>
<td>Increase in consumption, %</td>
<td>-27.9%</td>
<td>-6.7%</td>
<td>-17.9%</td>
<td>45.1%</td>
<td></td>
</tr>
</tbody>
</table>

Source: Annual Yearbook of Armenia

* Since data on Armenia has not yet been fully integrated into the EAEU’s shared database after the country's accession to the EAEU in early 2015, the values presented here have been taken from open sources and may be subject to correction.
Cement industry in Kyrgyzstan

Cement production in Kyrgyzstan was up 2.6% year-on-year in 2014. Cement consumption rose by 34.7% in 2013 compared with a year earlier. Increased new housing construction contributed to the growth in both cement production and consumption.16

The share of imports in total domestic consumption was 0.2% in 2013. Russia and Kazakhstan were the largest importers of cement manufactured in Kyrgyzstan. Kyrgyzstan exported 10.6% of domestic cement production in 2013.

According to the press office of the Kyrgyzstani Ministry of Energy and Industry, today the country has six cement plants with a total annual production capacity of 2.9 million tonnes17:

- OJSC Kant Cement Plant. The plant has an annual cement production capacity of 1.29 million tonnes and uses a wet process.
- CJSC South Kyrgyz Cement Plant. The plant has an annual cement production capacity of 1 million tonnes and uses a dry process.
- JSC Kurmentycement. The plant has an annual lime production capacity of 60,000 tonnes.
- LLC Technolin. Operations at the plant, whose annual cement production capacity is 320,000 tonnes, were suspended in 2009.
- LLC South Integrated Plant of Construction Materials. The plant has an annual cement production capacity of 200,000 tonnes and uses a mixed process.
- LLC Aksay Cement. The plant has an annual cement production capacity of 40,000 tonnes.

Table 7. The key indicators of the Kyrgyzstani cement market in 2009–14

<table>
<thead>
<tr>
<th></th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
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<tr>
<td>Output, thousands of tonnes</td>
<td>579</td>
<td>760</td>
<td>1017</td>
<td>1240</td>
<td>1676</td>
<td>1727</td>
</tr>
<tr>
<td>Imports, thousands of tonnes</td>
<td>207</td>
<td>50</td>
<td>42</td>
<td>0</td>
<td>3</td>
<td>н.д.</td>
</tr>
<tr>
<td>Exports, thousands of tonnes</td>
<td>9</td>
<td>3</td>
<td>95</td>
<td>126</td>
<td>178</td>
<td>н.д.</td>
</tr>
<tr>
<td>Consumption, thousands of tonnes</td>
<td>777</td>
<td>807</td>
<td>963</td>
<td>1114</td>
<td>178</td>
<td>н.д.</td>
</tr>
<tr>
<td>Imports, % of consumption</td>
<td>26.6%</td>
<td>6.2%</td>
<td>4.3%</td>
<td>0.0%</td>
<td>0.2%</td>
<td>н.д.</td>
</tr>
<tr>
<td>Exports, % of output</td>
<td>1.5%</td>
<td>0.4%</td>
<td>9.4%</td>
<td>10.2%</td>
<td>10.6%</td>
<td>н.д.</td>
</tr>
<tr>
<td>Increase in output, %</td>
<td>31.1%</td>
<td>33.8%</td>
<td>22.0%</td>
<td>35.7%</td>
<td>2.6%</td>
<td></td>
</tr>
<tr>
<td>Increase in consumption, %</td>
<td>3.9%</td>
<td>19.3%</td>
<td>15.7%</td>
<td>34.7%</td>
<td>н.д.</td>
<td></td>
</tr>
</tbody>
</table>

Source: Annual Yearbook of Armenia

16 minvlasti.ru.
17 Babylon.kg.

* Since data on Kyrgyzstan has not yet been fully integrated into the EAEU’s shared database after the country’s accession to the EAEU in early 2015, the values presented here have been taken from open sources and may be subject to correction.
Key trends in the EAEU’s cement industry

Russian and Kazakhstan rank first in the EAEU in the amount of cement produced using a wet process.18

The share of wet process cement totaled 63.6% in Kazakhstan, 56.7% in Russia and 31.5% in Belarus in 2014.

According to the survey, the capacity-utilization rates of Russian cement plants remain rather high (78.6% for wet processes and 64.9% for dry processes). The capacity-utilization levels of dry process cement plants have increased, from 54.0% in 2012 and 63.5% in 2013, a sign of ongoing industry modernization and the effectiveness of dry process technology.

Forty-eight percent of respondents believe that tight market competition will prompt manufacturers to close inefficient plants in the next five years. According to 36% of respondents, the current market trends send signals about the future consolidation of the industry as local manufacturers pursue more acquisitions to address key business challenges in the next three to five years, including technical modernization, cost cuts and growth in profitability.

Around 80% of respondents believe that the authorities should take a number of steps to support the robust and transparent development of the industry, including updating the Strategy for the Development of the Construction Materials and Prefabricated Construction Industries in the Period until 2020, drawing up a sub-program for the construction materials industry under the government program Driving Industrial Development and Competitiveness, approved by Directive of the Russian Government No. 328 of 15 April 2014, and initiating a federal-level program under the Strategy for the Development of the Construction Materials and Prefabricated Construction Industries.

Asked about government-initiated projects/programs that could substantially stimulate demand for cement in the next three to five years, 34% of respondents said that lower interest rates on mortgages could be an important driver. Other factors that could increase demand include the construction and renovation of roads (31% of respondents), the implementation of massive infrastructure projects, such as the construction of hotels and stadiums ahead of the 2018 World Cup (21%), and the development of port and airport infrastructure (14%).

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18 The survey excluded cement manufacturers in Armenia and Kyrgyzstan that are in the process of integration into the EAEU.

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Figure 6. Capacity-utilization levels of Russian cement plants by production technology in 2014 (%)

Source: EY

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Figure 7. Programs/projects that could drive demand for cement in the next three to five years

Source: EY
The cement industry in Russia, Belarus, Kazakhstan, Armenia and Kyrgyzstan in 2014–15
Mid-term cement industry outlook – survey results
Key issues surrounding Russia’s accession to the WTO and establishment of the EAEU

Russia’s key WTO accession commitments include:

- **Reducing import tariffs.** In line with its WTO commitments, Russia lowered the customs duty on cement from 5% to 3% in 2013. The rate remained unchanged in 2014 and 2015.
- **Eliminating and avoiding the reintroduction of quantitative restrictions on imports,** such as quotas, bans and permits, that could not be justified under the WTO provisions.
- **Applying the EAEU Generalized System of Preferences scheme for developing and least developed countries.** Under this scheme, cement imports originating from developing countries are subject to a lower customs duty (75% of the bound rate). The list of developing countries includes major exporters of cement to Russia, such as Turkey, Iran and China.
- **Joining the WTO Agreement on Government Procurement (GPA) within four years of accession to the WTO.** The GPA outlines government procurement rules and procedures to ensure the equal treatment of domestic and foreign suppliers competing for procurement contracts.
- **Eliminating all prohibited industrial subsidies** or modifying them so that any subsidy provided would not be contingent upon exportation or upon the use of domestic over imported goods.
- **Setting natural gas prices.** Producers and distributors of natural gas in Russia will set prices on the basis of normal commercial considerations while the authorities will continue to regulate prices for households and other non-commercial users.

What do cement manufacturers think about Russia’s WTO accession and the right of WTO members to apply trade defense measures?

When asked about the potential impact of Russia’s WTO accession on the domestic cement market, 44% of respondents expressed concern that tighter competition from imports could bring down cement sale prices.

Indeed, reciprocity and are fundamental principles of the WTO. However, the WTO rules permit a number of exceptions, such as the conditional right to apply trade defense measures. Such measures may be implemented along with tariff increases under defined emergency circumstances to protect the domestic industry from imports.

**Figure 8. In your opinion, which of the following has had or will have the most significant impact on your business following Russia’s accession to the WTO?**

- Tighter competition from foreign suppliers: 44%
- Lower cement sale prices driven down by increased imports: 39%
- Robust protection of the domestic industry aligned with consumers’ long-term interests: 6%
- Fewer administrative barriers due to the harmonization of industry-related regulations: 6%
- Others: 5%
Such contingent trade protection measures include:

- Anti-dumping measures
- Countervailing measures
- Safeguards

The first two types are applied in respect of a specific trading partner. The WTO permits members to impose them under defined circumstances, such as unfair competition as established by a thorough investigation. Such circumstances include the effects of export subsidies or dumping by partners.

In the first half of 2015, the EAEU applied five anti-dumping measures. Today, more than half of them are targeted at metals and automotive imports.

Countervailing measures, taken to counter the effects of export subsidies, are mostly applied by developed countries, with the US, EU Member States, Canada and Australia at the top of the list. Such measures are usually directed against China and India. Up to 15 new countervailing measures are introduced each year.

Safeguard measures are far less common. These are primarily applied by developing countries, mostly by India, Turkey, Jordan and Chile.

Analysts note an increase in protectionism globally

Countries around the world are increasingly resorting to trade-restrictive measures, as evidenced by recent statistics. Such measures are usually designed to spur business activity in a sluggish economy.

According to Protectionism’s Quiet Return, the Global Trade Alert’s report released in June 2015, on average two new measures were introduced globally each day between November 2008 and June 2015. Overall, more than 5,000 new trade-restrictive measures were implemented during the period. In 2015, BRIC countries accounted for nearly 40% of all existing discriminatory measures globally, which was almost double the 2008 level. According to the Global Trade Alert, the EU ranks first in the number of trade restrictions introduced around the world (with 604 measures), followed by India (452) and Russia (446). The largest number of restrictions has been enacted against China (1,745). China has taken restrictive actions against the US, Germany and Japan, while Russia has imposed trade restrictions against Germany, China and Ukraine. Russia faces the highest restrictions on its exports to India, Belarus and China.19

According to the WTO’s June 2015 and 2014 reports, between October 2014 and May 2015, the G20 countries introduced 119 new restrictive measures (17 on average each month), compared with 112 new measures enacted between November 2013 and May 2014.

As Figure 9 suggests, Russian manufacturers are concerned about cheap cement imports from Lithuania, Latvia and Poland. The flow of goods within the EAEU is steady overall, with competition largely limited to the shared cement market. Respondents also named Iran and Turkey among their key competitors. The majority of respondents do not expect the removal of sanctions against Iran to affect the cement market. Kazakh and Belarus cement manufacturers have a substantial presence in neighboring Russian regions within their logistical reach, in much the same way as Russian companies are present in Belarus and Kazakhstan. In addition, 82% of respondents noted that cement imports generally fall into the low-price segment.

According to the survey, India, China and Southeast Asia are the markets where cement demand is most likely to grow (72% of respondents), followed by the Middle East (14%) and North America (14%).

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19 vedomosti.ru.
Expansion of imports

Imports intensify price competition

Cement consumption in Russia increased by 1.88m tonnes in 2014, or 2.7%, from the previous year. The higher consumption levels in 2014 were due to increased domestic production, new housing construction and the implementation of large-scale infrastructure projects.

A rise in the share of cement imports in total domestic consumption in 2010–12 was followed by its sharp decline in 2013–14. According to CMPRO, imports accounted for 6.7% of total domestic consumption in 2014, compared with 7.2% in 2013 and 7.8% in 2012. This trend is attributable to increased domestic production that has satisfied domestic demand.

Around 50% of respondents said that the share of cement imports on the domestic market had decreased. Twenty-five percent did not notice any changes, while the remaining 25% said that imports had increased.

Commenting on the key drivers of imports, respondents pointed to foreign manufacturers’ lower costs, their geographical proximity to consumer markets and a favorable pricing environment on the domestic market.

Figure 12. In your opinion, how did the share of cement imports on the domestic market change in 2014 from the previous year?

- Decreased: 50%
- No change: 25%
- Increased: 25%

Figure 13. In your opinion, what factors are driving cement imports?

- Low production costs, foreign manufacturers’ geographic proximity to consumption markets: 43%
- Favorable pricing environment on the domestic market: 33%
- Impact of exchange rates on import prices: 10%
- High quality of imported cement: 10%
- Russia’s accession to the WTO: 4%

Figure 14. What do you think will be the market share of cement imports in 2015-16?

- From 4% to 6%: 42%
- From 2% to 4%: 25%
- From 10% to 15%: 17%
- From 8% to 10%: 8%
- Less than 2%: 8%
Today, there are no mandatory certification requirements for cement or any approved lists of certification bodies in Russia.

State Duma on 15 December 2002 provides for the introduction of mandatory certification for cement to ensure quality and the conformity of manufacturing, storage, transportation, distribution and disposal processes to technical guidelines, standards, rules and contractual terms.


Currently, according to the survey, only some of the imports are certified. Some importers obtain a certificate of conformity for an entire batch, providing only a sample, while others do not apply for it at all. This often paves the way for the importation of poor-quality materials.

Another important quality mark of cement is its conformity to construction specifications that vary across Russian regions. These include the alkali content (if inadequate, it may result in poor quality, including cracking, corrosion and the shortening of service life) and the tricalcium aluminate content (a higher content may affect freeze-thaw resistance).

Another critical issue is the level of quality assurance provided by certification bodies. There are over 100 independent accredited certification bodies in Russia that provide quality assurance and certification services. Certificates of conformity may be issued within one day, even though a proper quality assurance procedure should normally take at least two months.

According to 92% of respondents, quality control and certification processes for cement sold on the EAEU market did not change in 2014 compared with the previous year. Eight percent of respondents believe that control did improve.

Figure 15. Have your foreign competitors imported certified cement?

Figure 16. Did quality control and certification processes for cement sold on the EAEU market change in 2014 compared with 2013?
Many respondents highlighted the need to strengthen government control over certification bodies by adding cement to the Unified List of Products for Mandatory Conformity Assessment, tightening accreditation criteria, restricting the number of accredited certification bodies and establishing a laboratory setup requirement for them.

The nonprofit organization Soyuzcement is actively working on an initiative to include cement in the EAEU’s Unified List of Products for Mandatory Conformity Assessment (Certification). Soyuzcement insists that certification should be performed only by an accredited body.

In cooperation with the Eurasian Economic Commission, Soyuzcement, which was established to advance the interests of market participants, is pushing for quicker adoption of the EAEU’s Technical Regulations on the Safety of Buildings, Structures, Construction Materials and Parts, and is taking part in initiatives to develop a common industrial policy and intensify industrial cooperation between the EAEU member countries in line with the Resolution of the Supreme Eurasian Economic Council No. 40 of 31 May 2013, On the Major Priorities regarding the Coordination of the National Industrial Policies of the Republic of Belarus, the Republic of Kazakhstan and the Russian Federation. Soyuzcement is also involved in the development of a common methodology for assessing and forecasting trends in the construction materials industry, such as growth in cement consumption resulting from new housing and infrastructure projects in the EAEU.

Interestingly, 92% of respondents support the introduction of mandatory certification for cement sold on the EAEU market. They also back the proposal for adding cement to the EAEU’s list of products subject to mandatory conformity assessment followed by the issuance of uniform certificates of conformity.

Figure 17. In your opinion, what measures could help improve the quality control of cement sold on the EAEU market?

<table>
<thead>
<tr>
<th>Measure</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Including cement in the Unified List of Products for Mandatory Conformity Assessment</td>
<td>21%</td>
</tr>
<tr>
<td>Accelerating work to adopt the Customs Union's Technical Regulations on cement</td>
<td>15%</td>
</tr>
<tr>
<td>Tightening accreditation requirements for certification bodies</td>
<td>15%</td>
</tr>
<tr>
<td>Adopting an exhaustive list of certification bodies</td>
<td>13%</td>
</tr>
<tr>
<td>Establishing a laboratory setup requirement for certification bodies applying for accreditation</td>
<td>13%</td>
</tr>
<tr>
<td>Establishing requirements such as on-site checks, sample testing and inspections for certification bodies applying for accreditation</td>
<td>12%</td>
</tr>
<tr>
<td>Setting the minimum timeframes of quality assurance procedures for certification bodies applying for accreditation</td>
<td>11%</td>
</tr>
</tbody>
</table>
Trade in counterfeit products is one of the most challenging issues facing the EAEU cement industry. According to respondents, counterfeit bagged cement accounts for 19% of the market in Russia, 13% in Kazakhstan, 12% in Belarus and 3% each in Kyrgyzstan and Armenia.

Asked whether their company knew of any counterfeits of its own products on the market, 67% of respondents answered positively.

Forty-five percent of respondents believe that the share of counterfeit cement will shrink in 2015-16 while 36% expect it to remain at the same level, and 18% project its growth. However, experts warn that counterfeit cement production is growing at a faster pace than the production of bagged cement manufactured by accredited plants. The counterfeit industry is stealing market share from legitimate businesses while buyers are putting health and lives at risk by using fraudulent materials that adversely impact the safety and durability of structures.

As suggested by the survey, counterfeit cement accounts for 48% of cement sold privately, 26% of cement distributed by small construction companies and 11% of cement sold through DIY retailers.

Figure 18. What are your estimates of the share of counterfeit bagged cement in the EAEU countries in 2014?

Figure 19. What was the share of counterfeit bagged cement in each of the primary distribution channels in 2014?
Market experts say that counterfeiters usually go unpunished, pointing to insufficient regulatory controls and an inadequate punitive approach that together make the fight against counterfeiting ineffective. Our respondents agree. Among the measures that could enhance the fight against counterfeiting, industry players named the following:

1. Establishing mandatory certification for cement to provide an assurance of quality. Currently, certification in the cement industry is voluntary. The introduction of a mandatory requirement would reduce the risk of harm or damage to people, property and the environment, as well as help protect consumers from deceptive practices. Mandatory certification is critical for effective control of goods before they enter the market.

2. Adopting and enacting the EAEU’s Technical Regulations on the Safety of Buildings, Structures, Construction Materials and Parts. Such regulations would harmonize the technical requirements for the product, provide better protection for the EAEU market, and help rights-holders fight against manufacturers and sellers of bad-quality cement by holding them liable for the failure to meet technical specifications.

3. Amending the Russian Administrative Offenses and Criminal Codes to tighten penalties for offenders and strengthen law enforcement practices, as well as establishing more stringent oversight over local production and conducting campaigns to raise manufacturers’ awareness of measures against counterfeiting.

4. Increasing cooperation with consumers’ associations and the Federal Service for Consumer Rights and Human Welfare (Rospotrebnadzor). Currently, Rospotrebnadzor is not allowed to inspect plants or retailers without warning them in advance of the coming inspection and without receiving a complaint from a consumer or a consumers’ association, which makes such control mechanisms utterly ineffective. It is perfectly feasible for cement manufacturers to unite with consumers’ associations to make sample purchases and submit their findings to Rospotrebnadzor.

What do respondents think?

The adoption of the EAEU’s Technical Regulations on the Safety of Buildings, Structures, Construction Materials and Parts will help harmonize technical requirements for products and provide better protection for the EAEU market, as well as allow rights-holders to effectively fight manufacturers and sellers of bad-quality cement.
The key challenges facing domestic cement producers include the high cost of debt, rising energy tariffs, a low sale price per tonne of product vs. the high cost of production, and competition from imported supplies. All of these challenges make the industry less attractive for investment.

A resilient focus on improved technical capabilities and higher production efficiency are set to become key determinants of competitive success over the next three to five years. Only those players that have embraced modernization will be able to maintain their competitive advantage in the long term.

One of the steps toward better efficiency, attractiveness and responsibility is switching to alternative energy sources -- which are not now nearly as common in the EAEU as elsewhere in the world.

Our 2015 survey suggests that alternative energy sources (peat, household waste, shredded tires, wood chips, etc.) account for only 6% of the total energy mix of the EAEU’s cement industry. This stands in stark contrast with Germany, where alternative energy consumption saw a remarkable rise from 4% in 1987 to 63% in 2014. As seen in Figure 23, as early as 1990, alternative energy made up 7% of total energy consumed by German cement producers.

While major EAEU players have been looking closely into this issue, they still face difficulties in developing alternative energy sources and diversifying their energy mix. For example, producers willing to increase the use of alternative fuels should invest heavily in controls over the acceptance, storage, refining and supply of these fuels, and make sure that both the amount and quality of such fuels are sufficient (millions of tonnes of fuel with a calorific value no lower than 4,000 kcal).
The survey suggests that half of the respondents plan to optimize costs by switching to alternative energy sources while others are still debating the issue (25%) or do not plan any cost optimization initiatives (25%).

According to respondents, the wider adoption of alternative fuels is restricted by the excessive costs of implementing the relevant technologies, a dearth of suppliers, high prices, licensing difficulties and the low economic efficiency of such fuels.

Furthermore, it is critical that regulations requiring mandatory on-site disposal be developed and introduced for specific types of waste generated in cement production. A variety of dangerous and unusable materials are left over after waste collection and recycling, including ash, sludge, vegetable residues, bone flour, textile wastes, leather waste and so forth, which are non-recyclable and must be prepared for burning. Another priority is to take legislative measures to prevent the emission of hazardous wastes and to ensure that these are burned in kilns at cement plants, with the disposal costs to be borne by the companies or individuals generating such wastes.

Clearly, without wider support from the Government and revisions to the regulatory landscape, cement producers will not be able to drive change. The industry's sustainable development must, therefore, be driven by a joint and concerted effort of all stakeholders to increase the use of alternative fuels gradually, over time.

Looking at changes in key production costs from the previous year, the highest increase was seen in depreciation costs (up 28.3%), while the cost of debt (bank and other loans, leasing and factoring) rose by 18.4%.

Transportation costs make up roughly 18% of the selling price of cement. According to CMPRO, in H1 2015, cement transportation by rail was 13.6m tonnes, down 14.7% y-o-y. While the volume of rail traffic was quite substantial in absolute terms, it accounted for only 46% of total tonnes moved in H1 2015, with the remaining 54% dispatched by road. Cement transportation by road is thus gaining significance when it comes to analyzing changes in supply and demand.
Our survey suggests that 56% of cement deliveries were made by rail and 44% by road. The distance of delivery varies between 120km and 2,000km, with an average distance of less than 600km for deliveries by rail and 400km by road.

Apart from rising transportation rates, cement producers encounter a number of other issues when using rail transport. These include rail capacity limitations (27%), seasonal traffic fluctuations (18%) and shortages of rolling stock (9%).

The switch to road transport is viewed by 69% of respondents as the most realistic solution to the transportation issue, while 23% favor government support for specialized rail-car builders and 8% say that the best solution would be to purchase or lease their own rolling stock.

Faced with growing competition in the EAEU marketplace, cement producers are seeking ways to reduce and optimize costs. According to the survey, 42% of respondents reduced their costs in 2014 and expect to benefit from these efforts in 2015, while 28.6% of respondents plan to reduce costs in 2015–16, and 28.6% have already reaped the benefits of the cost-cutting steps taken in 2014.

These cost-cutting initiatives mainly involve fixed asset repairs (28% of respondents), electricity and gas costs (17% and 14%, respectively), and a switch to cheaper means of transport (17%).

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**Figure 25. By how much did key production costs grow in 2014 over the previous year?**

- **Depreciation**: 28.3%
- **Cost of debt (bank and other loans, leasing and factoring)**: 18.4%
- **Gas**: 7.2%
- **Labor costs, including payroll and social contributions**: 6.4%
- **Electricity**: 5.4%
- **Other energy**: 2.8%
- **Fixed asset repairs**: -0.9%
- **Road transportation**: -3.0%

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**Figure 26. What are the most realistic solutions to the transportation issue?**

- **Switching to road transport**: 69%
- **State support for rail-car builders**: 23%
- **Purchase or lease of own rolling stock (a locomotive and cement carriers)**: 8%

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**Figure 27. How has your company approached cost-cutting?**

- **We cut costs in 2014; the impact on our results is anticipated in 2015**: 42%
- **We plan to cut costs in 2015–16**: 29%
- **We cut costs in 2014 with an immediate impact on our results**: 29%
Industry growth prospects

The outlook for the growth of the cement market in 2015 varies greatly, from 10% and more (33% of respondents), to 5%-10% (25% of respondents) and 1%-3% (17% of respondents). The forecasts for 2016 are more conservative. Half of the respondents said growth may reach 5%, while the remaining respondents were split equally between those expecting no change from 2015 and those anticipating growth at 3%-5%.

With higher product prices and growing competition anticipated in the near term, producers are now focused on cost reduction and capacity improvements, as well as on retaining and increasing their market share.

Impact of sanctions

When asked about the economic sanctions and their impact on domestic cement production, 90% of respondents agreed that their business is affected by the sanctions in one way or another. Seventy percent of those surveyed believe that the demand for their products has declined in response to the weaker ruble and rising cost of debt; 20% face difficulties in implementing plant upgrade and expansion projects due to the higher prices of imported equipment; and only 10% say the impact of the economic sanctions on their business has been moderate. More than half of the respondents believe the sanctions will continue to weigh on the industry in the next two years.

Figure 28. What changes do you expect in your market in the near term (the next 1-3 years)?

- Higher prices for products: 26%
- Growing competition: 24%
- Rising demand for products: 13%
- Mandatory certification for all products: 11%
- Decreasing product imports: 11%
- Falling demand for products: 8%
- Lower prices for products: 4%
- Increasing product imports: 3%

Figure 29. Have the economic sanctions and/or restrictions affected your business in Russia?

- Yes, demand has declined in response to the weaker ruble and rising cost of debt: 70%
- Yes, we face difficulties in implementing upgrade and expansion projects due to the higher prices of imported equipment: 20%
- Yes, moderately: 10%

Figure 30. Which of the following best describes your company’s plans for the next three years?

- Cost reduction: 25%
- Plant upgrades: 17%
- Gaining market share: 14%
- Retaining market share: 11%
- Organic growth: 11%
- Improved profitability: 11%
- Headcount reduction: 5%
- Partnering and joint ventures: 3%
- Growth through M&A: 3%
Industry consolidation

According to expert estimates, the presence of several independent players suggests that further consolidation within the EAEU is quite likely. As a result, cement producers will seek to scale up their production and attract significant investment into the aging assets that need upgrading. Consolidation in the cement industry should also support higher prices, with new players emerging as the dominant monopoly in their local markets.

About half of those surveyed say they have no plans to expand into new regions, as opposed to the other half, who view the Central, North West, South, Volga and Siberian Federal Districts of Russia, as well as Kazakhstan and Belarus, as the most attractive destinations.

Investment objectives

How do cement producers plan to spend their own and borrowed funds? As their priority investment objectives, most respondents mention cost reduction initiatives, as well as the refurbishment, upgrading or more efficient use of production facilities. These are followed by changing the product mix and expanding into new geographies/markets.

Figure 31. How will the cement market develop over the next five years?

- The market will encourage producers to close down low-performing assets: 48%
- The market will encourage local producers to acquire other players and to consolidate the industry: 36%
- The market will encourage local producers to expand into new markets: 8%
- The market will encourage local producers to expand production capacity: 4%
- The market will encourage international cement manufacturers to acquire local players: 4%

Figure 32. What are your company’s priority investment objectives?

- Reduce production costs: 28%
- Improve the performance of existing production facilities: 28%
- Refurbish or upgrade existing production facilities: 16%
- Change the mix of existing products and services: 16%
- Expand into new geographies/markets: 4%
- Acquire other players: 4%
- Build new production capacity (wet process): 4%
Sources of financing

Survey participants noted the rising cost of debt (56%) and difficulties in raising debt capital (44%).

As access to debt capital becomes tighter, 46% of respondents are considering using equity to finance business expansion and capacity upgrades.

While many respondents mentioned the deterioration in bank lending terms, 29% of survey participants continue to view bank loans as a possible source of funding to maintain and upgrade their production assets.

About 17% of respondents believe that equipment leasing is also of interest to producers.

Note that the 2013 survey revealed stronger interest in bank financing (35%), with equipment leases being favored by only 13% of respondents.

Figure 33. How has the availability of loans in 2014–15 changed, compared with previous periods?

Figure 34. What sources of financing is your company considering for expansion?
Tax factors

The major tax issue industry players are currently facing is the need to restructure their business to comply with the new de-offshoring regulations, which came into effect on 1 January 2015.

A key change triggered by the de-offshoring campaign is the introduction of new concepts, such as a controlled foreign company (CFC) and tax residence for legal entities and the actual recipient (beneficial owner) of income.

A CFC is defined as a foreign company that is not tax-resident in Russia and that is controlled by individuals and/or legal entities that are Russian tax residents. Controlling persons are those individuals or legal entities that hold more than a 50% interest in the controlled entity. Under the CFC rules, controlling persons are obliged to pay tax on any income earned by the CFC in a given tax period that has not been distributed as dividends. The rules also provide for tax exemption if certain criteria are met.

Another major change is the introduction of criteria for determining the tax residence of foreign companies by place of effective management. A company’s place of effective management will be considered to be Russia if a relative majority of the meetings of its board of directors are held in Russia or if its executive body and executive officers perform their duties in relation to that company in Russia. In addition to those mentioned, there are also other criteria that may be used to determine the place of effective management.

A beneficial owner of income is an individual or a legal entity that has the right to use or dispose of that income by virtue of ownership or control of the company or by virtue of other circumstances. This concept provides for the application of a look-through approach, whereby the withholding tax rate on Russian-sourced income is determined in accordance with the provisions of the relevant tax treaty between Russia and the beneficial owner’s country of residence.

Given the above regulatory changes, cement industry players are revising their corporate governance and financing frameworks in order to identify potential exposures and restructure their businesses so that the income of their foreign group entities is not taxed in Russia.

Another change involves amendments to the federal law, On the Contract System for the Procurement of Goods, Work and Services for Public and Municipal Needs, which were introduced on 13 July 2015. Under the amended legislation, companies from jurisdictions that have been included by the Finance Ministry on the list of countries and territories offering a preferential tax regime and/or not requiring the disclosure or provision of information may not bid for public procurement contracts. The new rules do not apply to Russian subsidiaries of foreign companies although this restriction was previously contemplated.

Regulations dealing with transfer pricing, as well as tax relief and preferences for investment projects, still have a major impact on the business of cement producers. The first arbitration decisions have been handed down in cases initiated following transfer pricing audits by the tax authorities that give an idea of the approaches taken by the tax authorities and courts. In addition, recent changes to the property tax calculation rules have promoted a wave of litigation over the use of the given property’s cadastral value in such calculations.
Moving toward greater efficiency and transparency

The majority of survey participants named energy efficiency, product quality and labor safety as top corporate social responsibility (CSR) objectives.

Reducing the level of emissions and expanding employee benefits continue to play a prominent role in the CSR agenda.

A hefty percentage of those surveyed recognize the importance of increasing transparency for external stakeholders (industry partners, consumers, local authorities and communities) across all their geographies. To achieve transparency, it is critical to improve both financial and nonfinancial reporting that will provide greater visibility to all stakeholders into both the challenges and opportunities across the value chain, including product quality, environmental protection, occupational safety, social security and support for major infrastructure projects.

According to the survey, leading industry players promulgate initiatives to promote CSR among their suppliers and business partners.

Figure 35. What aspects of CSR/sustainable development will be the focus of your activities in 2015–16?

<table>
<thead>
<tr>
<th>Aspect</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>More efficient use of resources (including energy resources)</td>
<td>18%</td>
</tr>
<tr>
<td>Engagement with customers on product quality issues</td>
<td>16%</td>
</tr>
<tr>
<td>Labor and industrial safety</td>
<td>11%</td>
</tr>
<tr>
<td>Reduced air emissions</td>
<td>10%</td>
</tr>
<tr>
<td>Social security benefits (social package)</td>
<td>8%</td>
</tr>
<tr>
<td>Engagement with suppliers on CSR/sustainable development</td>
<td>8%</td>
</tr>
<tr>
<td>Greater transparency of business</td>
<td>5%</td>
</tr>
<tr>
<td>Sponsorship and charity</td>
<td>5%</td>
</tr>
<tr>
<td>Land restoration</td>
<td>5%</td>
</tr>
<tr>
<td>Protection of biological diversity</td>
<td>5%</td>
</tr>
<tr>
<td>Waste disposal</td>
<td>3%</td>
</tr>
<tr>
<td>Employee rights</td>
<td>3%</td>
</tr>
<tr>
<td>Corporate volunteering</td>
<td>3%</td>
</tr>
</tbody>
</table>
Best available techniques: from vision to reality

Burning platform to drive best available techniques

A substantial part of domestic production is not currently competitive on the global market. There are also a number of objective factors that will impact profitability in the mid to long term, including the following external and internal factors:

- Constantly rising energy tariffs
- Depreciation and obsolescence of most production assets
- Substantial capital investments in the upgrading of core production facilities

The low level of technology engagement, coupled with market and institutional barriers faced by Russian companies, impacts the competitiveness of local manufacturers. With the current state of production assets remaining unchanged, the domestic economy is set to lose momentum as macroeconomic risks rise and the impact on the environment becomes increasingly stronger. By 2020, the excess emissions fee will go up, as stated in Federal Law No. 219-FZ of 21 July 2014, On Amendments to the Federal Law on Environmental Protection. The higher fee will have a negative impact on the financial position and cost profile of local producers. Along with the resolution of systemic institutional issues, the upgrading of production capacity is therefore a priority target in Russia’s industrial policy.

The key mid-term objectives of the country’s environmental policy include regulating the total allowable impact on the environment by reference to best available techniques (BAT). This approach would be a vehicle for improving the competitiveness of domestic producers.

What is a best available technique?

A best available technique means the most advanced method of manufacturing goods, performing work or providing services that is both technically implementable and effective in achieving environmental goals through reliance on the optimal set of criteria. BAT are principally aimed at enhancing the quality of process management and controls across production companies to guarantee the adoption of a comprehensive approach to environmental protection. They are viewed as the right tool for improving process efficiency and raising environmental safety levels at production facilities.

The amendments to Federal Law No. 219-FZ create a framework of economic incentives for reducing pollutant emissions and discharges. Any company looking to upgrade its production facilities may borrow money from a dedicated industry support fund. The amended law provides for a gradual increase in the environmental charge and offers a system of integrated environmental permits for those businesses that have an environmental efficiency program in place. The law also introduces the state environmental review process for major infrastructure projects.

The Government plans to release 48 BAT reference documents in the period from 2015 to 2017, with 10 documents describing advanced processes, techniques and methods for preventing and mitigating the negative impact on the environment to be developed as early as 2015.

BAT adoption in the cement industry: an urgent priority?

While being fairly competitive in Russia, domestic cement producers lag behind their international peers. The key factors affecting the competitiveness of local industry players include the energy-intensive wet process, exacerbated by rising energy bills and a lack of the conditions needed for implementing upgrades. Such conditions would include access to finance, government support for industry players and measures to stimulate exports and reduce transportation rates. The industry’s development is also hampered by lackluster growth in construction and an overall economic downturn.

The competitiveness of the domestic cement industry may be improved by taking a number of concerted steps aimed at stimulating the development of the raw materials base, wider use of recycled materials, technology upgrades and higher energy efficiency in production.

According to analysts from Soyuzcement, a number of the Government’s strategic initiatives focused on the construction materials industry (e.g., Strategy for Developing the Construction Materials Industry and the Construction Materials Industry Road Map that forms part of a wider state program of industrial development and enhanced competitiveness) may spur the future growth of the domestic cement industry. Other measures to support the cement industry include mandatory certification, the destruction of counterfeit product and the adoption of BAT. Together, these efforts will boost the competitiveness of local players and stimulate investments in production upgrades.

21 Vedomosti.ru.
In 2008–14, the cement industry grew at an annual rate of 7%, with the addition of 30 million tonnes of dry capacity. This helped to reduce fuel and energy consumption (from 205 to 114 kilos per tonne, and from 130 to 110 kWh), as well as to increase labor productivity (from 1,500 to 4,000 tonnes per person per year), with the resulting cumulative impact on the environment reduced by 60%.

The resilient growth in Russia’s cement industry signals the upcoming shift to BAT. In addition to a reduced negative impact on the environment, the application of BAT is a strong driver toward technological advancement.

A BAT reference document may help cement plant executives to assess their current level of emissions and discharges and to apply for a compliance certificate on a voluntary basis before integrated environmental permits are introduced in 2019. The compliance certificate confirms that the holder’s production process is environmentally safe and contributes to its competitive position on the market.

**Environmental performance levels: criteria set in BAT Reference Document on the Production of Cement**

There are various technologies used to produce cement, each of which requires different amounts of fuel (heat), electric energy and natural resource consumption. The production of cement causes the emission of a range of pollutants that have a negative impact on the environment.

Pursuant to Federal Law No. 219-FZ of 21 July 2014, On Amendments to Federal Law on Environmental Protection and to Certain Regulatory Acts of the Russian Federation, environmental performance is measured based on pollutant markers that are established to control the current level of pollution, depending on the technologies and processes applied.

**Figure 36. Main cement production emissions**

<table>
<thead>
<tr>
<th>Phase</th>
<th>Activity</th>
<th>Pollutants</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Storage and preparation of raw materials and fuels</td>
<td>Dust, acid gases, organic substances, volatile metals, dioxins, noise</td>
</tr>
<tr>
<td>2</td>
<td>Clinker burning</td>
<td>Dust, noise</td>
</tr>
<tr>
<td>3</td>
<td>Cement grinding</td>
<td>Dust, noise</td>
</tr>
<tr>
<td>4</td>
<td>Cement storage, packaging and dispatch</td>
<td>Dust, noise</td>
</tr>
</tbody>
</table>

Source: Survey Criteria for Selecting Environmental Performance Benchmarks in BAT Reference Document on the Production of Cement

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Drawing on the European experience of devising BAT reference documents, the following benchmarks are proposed:

- Consumption efficiency – a set of general metrics that have a significant impact on the efficiency and environmental safety of cement production. These include the following:
  - The consumption of raw materials required to produce one tonne of Portland cement clinker or one tonne of Portland cement (which relates directly to the resource intensity of cement production)
  - The consumption of heat (fuel) required to burn one tonne of Portland cement clinker (which reflects the fuel intensity of cement production)
  - Consumption of electricity required to produce one tonne of Portland cement (which reflects the energy efficiency of cement production)
- Emissions – the release of substances, vibrations, heat or noise typical in cement production that have major harmful effects on the environment or human health.

These include the following:

- Emissions of air pollutants
  - i) Dust emissions
  - ii) Nitrogen oxide (NOx) emissions
  - iii) Sulfur dioxide (SO2) emissions
  - iv) Carbon monoxide (CO) emissions
- Noise emissions

Given that emissions cause the majority of damage to the environment, emission data is the most meaningful source of information for measuring environmental impact. By carefully analyzing both emission data and consumption levels, cement manufacturers will be able to compare various options and determine the best available technique that would help to minimize their environmental footprint.

**BAT globally**

There are 33 reference documents (BREFs) that were developed in the EU with a view to promulgating BAT and establishing quality standards for individual industries. Rather than imposing the use of an “appropriate” technique, BREFs propose selecting those techniques that best meet the permitted range of emission and waste generation levels.

BREFs may be broadly divided into two categories: vertical and horizontal. Vertical BREFs are specific to a type of industry or a combination of industries, as opposed to horizontal BREFs, which are generally relevant to the majority of industries.

Below are the key enablers for improved environmental performance of BAT adopters:

- Tight regulatory requirements
- A ready-to-use, approved tool
- EU-wide environmental monitoring programs
- Incentive mechanisms
- Data transparency
- Urban environmental programs.

Globally, BAT are viewed as a proven, hands-on tool to control the environmental impact caused by industrial activities.

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