

I. Introduction.

Reasons for the submission of the proposal

Search for strategic partner to take part in building the mineral water bottling plant on the base of certified drill hole of table mineral water “Naftusya” type.

II. Project information.

Project name.

Building the mineral water bottling plant on the base of certified drill hole of table mineral water “Naftusya” type.

Submitted by.

“Ester” ltd, Ukraine, Ternopil, Grushevskogo str, 16.

Topic.

Producing the table mineral water “Naftusya” type.

Region

Ukraine, Ternopil region

Contact person.

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Head of enterprise.

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III. Compliance with Business-Award Criteria.

1. Project description (one page only).

“Ester” ltd is searching for the potential partner for building the mineral water bottling plant on the base of certified drill hole of table mineral water “Naftusya” type in the smt. Pidvolochysk Ternopil region, Ukraine. The company is interested in the cooperation with foreign partner which would be able to provide the equipment needed for bottling the mineral water. Its installation and further exploitation would be launched in the reconstructed building with 600 square meters area.

The possible legal form of cooperation – the joint company establishment, equipment leasing, organization of joint production through the signing the agreement about joint activity etc.

At the present “Ester” ltd owns a plot of land with 1000 square meters area with all necessary infrastructure, where the certified drill hole of mineral water “Naftusya” type with 50 millions litres/per year production capacity is situated. This table mineral water contains the biologically active ingredient – organic matter, rich in iodine, bromine, copper, manganese, fluorine, iron and others microelements, which is proved by the certificate issued by Ukrainian SEI MRC of the Ministry of Health Protection in Odessa.

Mineral water “Naftusya” type has a clearly stated medical effects in treating the gastrointestinal, endocrine and others internal diseases. Ukrainian scientists discovered also positive effects of its properties in treating the diseases caused by radiation, such as restoring the blood circulation, cerebral blood flow etc.

The main financial characteristics of the project and the indicators of the economic efficiency are:

- total cost of the project – **\$ 643 000**, including: cost of already bought building and land - \$ 110 000, buying the PET-bottles production line- \$80 000, mineral water bottling line – \$ 448 000 (**\$350 000** investor’s financing and \$ 98 000 company’s own recourses), equipment installation and starting work cost- \$5 000.

- amount of investment needed – **\$ 350 000.**
- planned production capacity – 3-3,5 million liters per year
- economic efficiency (profitability) – 26.1% (according to the calculation below)
- payback period – 28 months.

The competitive advantages of this project are:

- reduced risk level explained by the company substantial experience of operating on the food and drinks whole trade market, existing of strong distribution network.
- stable market growing (constant increase of mineral water sales and consuming volume from year to year).
- high profitability and short payback period;
- high quality of mineral water, provided by producing and packaging in the same premises and avoiding transportation (without the special packaging mineral water loses its quality characteristics after about 40 km of transportation).

2. Company

“Ester” ltd was founded in 1999, the main activity – operating on the food and drinks whole trade market. During the time of its existence company expanded the range of its activities and launched the small production and packaging of different kinds of pasta and other macaroni, after acquiring necessary equipment. It is also the regional representative for such a big companies as “Kyiv-Konti”, “ABK”, “Svitoch” etc.

The main participants of company Statute Fund are Maksymiv Petro Ivanovych (60% of statute fund contribution) and Lypovets Volodymyr Stepanovych (40% of statute fund contribution).

The company’s turnover for last reporting financial period (last three months)- 1 150 thousand hryvnas (about \$ 227 720), profit – 86 thousand hryvnas (\$ 17 020). For the nine months of current year those financial indicators were accordingly 3 745 and 54 thousand hryvnas (\$741 580 and \$10 690), which exceed the turnover and profit for same period (9 months)of last year on 13% and 8 %. According to the financial results statements for the past 5 years the company’s activity was profitable.

3. Product or service.

Mineral table water “Naftusya” type is very popular on the Ukrainian market, has a strong reputation for its valuable preventative and therapeutic assets and the consumers demand for it is constantly growing.

The chemical type of mineral water content is hydrogen carbonate with calcium, magnesium and sodium microelements and level of mineralization 0,9-1 gr/dm³ . This table mineral water contains also the biologically active ingredient – organic matter, rich in iodine, bromine, copper, manganese, fluorine, iron and others microelements, which is proved by the certificate issued by Ukrainian SEI MRC of the Ministry of Health Protection in Odessa.

Mineral water “Naftusya” type has a clearly stated medical effects in treating the gastrointestinal, endocrine and others internal diseases. Ukrainian scientists discovered also positive effects of its properties in treating the diseases caused by radiation, such as restoring the blood circulation, cerebral blood flow etc.

Mineral water with the high level of biologically active organic elements (Naftusya, Zbruchanska and Novozbruchnska types) are widespread in the Ivano-Frankivsk, Lviv, Ternopil, Chernivtsi and Khmelnytsk region. The same type of mineral waters brought the Truckavets resort its well-known reputation as the best health and spa resort in Ukraine. Also this type of mineral water is used in others health resorts in Sataniv, Shidnytsa , such a well-known sanatorium institutions as “Ukraine” (Khmelnysk region), “Zbruch” (Ternopil region).

The quality of mineral water depends not only on its chemical content and on the physical and chemical characteristics of its active ingredients but also on the containers, used during the transportation and packaging. If the containers used were not specially treated, mineral water loses its quality properties after about 40km of transportation. According to the Department of the State Standard Authority data, from the 705 different kinds of mineral water, available on the Ukrainian market, 175 kinds are low-quality because they are transported to the bottling plants in the unsuitable containers. In the ideal scenario mineral water suppose to be produced and bottled on the same premises.

High quality provided by producing and bottling the mineral water directly near the source, low net cost of the product, possible because of avoiding the transportation expenses are the main competitive advantages of the product.

At present the company has all the necessary documents, permits and licenses for producing and bottling the mineral water (certificate issued by Ukrainian SEI MRC of the Ministry of Health Protection in Odessa, license for the part of water field exploitation, Regional SES conclusion etc). Patent for using its own mineral water brand "Kryshtaleva" is pending.

The set of equipment needed for bottling the mineral table water in the PET-bottles includes:

- machine for filling the bottles rotary type XRB-6 with the production capacity of 1800-4000 bottles per hour;
- carbonator (for mixing the water and carbonic acid) KOMI -45 with production capacity 4500 liters per hour;
- semiautomatic machine for packaging PET- bottles in sets with shrinkable film with production capacity 600 packages per hour;
- conveyer belt with 1,5kbt capacity and 10 meters long
- equipment for purifying the mineral water from chemical, mechanical and bacterial pollution with production capacity 100-230 cubic meters.

Because of product high quality, carefully planned marketing policy, stable market growing, mineral water "Kryshtaleva" will gain the popularity and customers loyalty.

So, "Ester" ltd is going to produce the next range of products:

- *still mineral table water in the PET-bottles:*

- 0,5 liter bottle
- 1,5 liters bottle
- 5,0 liters bottle
- 15 liters container.

- *sparkling mineral table water in the PET-bottles:*

- 0,5 liter bottle
- 1,5 liters bottle
- 5,0 liters bottle

- *still mineral table water in the glass bottles (0,33 liter)*

- *sparkling mineral table in the glass bottles (0,33 liter)*

4. Market and competition overview.

There are 84 mineral water fields in Ukraine. The volume of known reservoirs in the country is 2,4 millions square km. The level of exploitation of the underground fields doesn't exceed 2,5%.

Mineral water production and consumption is increasing every year.

13-25% growth in the year describes the dynamic development of mineral water market. The group of leading operators is formed already (80% of market volume consist of the output of 15-20 main producers).

Dynamics of mineral water production 2001-2005 years (State Statistics Committee).

Period	Volume of output, thousand dal.	Percentage of increase\decrease.%
2001	64 670	
2002	81 176	25,5
2003	93 046	14,6
2004	91 083	-2,2
2005	102 839	13,0

The growth rate of production volume is quite high. Small decrease was reported in 2004 because of seasonal aspects (particularly cold summer). During the 2001-2005 period the production output has grown on 59% from 64.7 million dal to 102.8 million dal which in the money equivalent 1,7 billion gryvnas (\$34 millions). The main reason of this growth was increase of consumption capacity and interest in healthy products.

Plenty of experts observe the stabilization of mineral water market. Their opinion is based on the growth rate slowing down within 2003-2005.

Average consumption of mineral water (per year per person), liters (2004(State Statistics Committee)

Country	Volume of consumption
Italy	140
France	112
Germany	100
Czech Republic	84
Bulgaria	33
Ukraine	21
Russia	11

At present Ukrainians drinks about 26 liters of mineral water per year, in 2003 this amount was 21 liters, 2003- 17,6 liters. But we still have long way to go – average Europeans drinks about 130-150 liters per year .According to this data it is possible to suggest that the mineral water intake per person will increase at least three times. The same applies to the production – for example in Western Ukraine the capacity of recourses allow to increase the output in 5 times.

The main operators on the market.

There are about 350 companies producing mineral water on the Ukrainian market. Nevertheless only 15-20 big companies control up to 80% of it.

The main producers of mineral water (2003-2005 years) (AC Nieslen).

Company's name	Share of the market, %		
	2003	2004	2005
IDS Group Myrgorodska”, “Morshynska Borjomi”	17.9	20.9	23.1
Coca-Cola	6.5	6.8	7.8

“Bon-Aqua”			
JSC “Erlan” “Biola Znamenivska	5.4	6.1	7.0
Ukrainian mineral waters “Kuyalnyk”	4.2	3.6	5.1
JSC “Obolon” “Obolonska”	4.7	4.6	4.4

In 2005 the new company **IDS Group** become undeniable leader with more than 20% of the market in control. It was created in 2004 by merging the biggest mineral water producers and distributors: Myrgorod mineral water plant, Morshyn mineral water plant “Oskar”, JSC “Industrial and distribution systems” and JSC ‘Nova’. The joint company produces and sell wide and popular range of mineral water produced in ecologically clean recreation regions of Ukraine (“Myrgorodska”, “Morshynska”, “Staryy Myrgorod”, “Alyaska”, “Sorochynska” etc) and also imports popular “Borjomi” from Georgia.

The most popular brands in 2005 were (AC Nielsen) :

Name of the brand	Share of the market,%
Myrgorodska	9
BonAqua	5.7
Biola Znamenivska	5.6
Obolonska	5.4
Sofia Kyivska	4.3
Tsarychanska	3.7
Polyana Kwasova	3.7
Truskavetska	3.4
Morshynska	3.2
Luzchanska	2.8
Others	53.2

Market tendencies

Reduction of small producers market share.

The vulnerability of small and medium companies oriented only on local market is explained by the specifics of their work – they produce mainly spring and table water, consumption of which changes depending on season. Basically those companies increase their output only during the peak season and don’t pay enough attention to developing the effective and stable distribution channels. Last year, when the seasonal change in demand wasn’t very significant, accordingly to the experts opinion, the market share of small producers decreased on 30%. But there was no sizeable change in market share of big companies. Their output is growing steadily with the stable rate every year.

At the same time there is a tendency to some middle companies strengthening their positions on local markets.

Range extension and the changes in consumer’s taste.

Dynamics of mineral water sales (by categories) :

Years	Classification by kinds (% from total sale)		Classification by mineralization level%			
	still	sparkling	medicinal	table-medicinal	table	others
2003	8,8	91,2	36,7	38,7	15,8	8,8

2004	12,4	87,6	35,1	34,2	18,3	12,4
2005	15,5	84,5	28,6	31,5	24,7	15,2

The experts explain the growth of table water sale by active advertisement campaign and the growing culture of mineral water consumption. The customer is much better informed about the differences between table-medicinal and table waters and according to producers opinion the tendency of growing demand for table water will stay for next few years.

Also there is the extension of still water section of the market. Almost all big producers included still mineral water in their range even though this means some technological difficulties and additional costs. At the moment the percentage of still water in total production isn't sizeable, most companies produce it just for range extension. But in most western European countries (France, Italy, Spain etc) the still mineral water makes up to 50-80% of their mineral water market. In Ukraine it makes only 15.5% and continues to grow.

According to AC Nielsen research, last year the demand on sparkling mineral water has grown on 17%, still- 38%. "Coca-Cola Beverage Ukraine" increased its production of still water on 10%, "Dobra voda" ltd – on 40%.

Most of companies extended its range by adding flavoured mineral water. But it seemed to have only short lasted effect – the short term sales increase occurred, but after few months demand went down. But some companies, for example "Obolon" keeps and expand its range of flavoured mineral water.

Strong position is spotted in sales of new product: mineral water enriched in microelements and silver ions (TM 925), which was introduced on the market by Donetsk company "Olymp".

The package plays a significant role as well. The companies oriented on home and office delivery market produce 5,10 and 20 litres bottles, there is also increase of the glass bottles production, preferred by restaurants and bars, but most popular is still 0,5 and 1,5 litres bottle packaging.

So, all those tendencies have defined the structure of mineral water market, dividing it on clear section and demanding strong company positioning.

New submarket (HOD- home and office delivery, catering and retail chains delivery etc) caused the appearance of new and expanding of the old distribution channels. The most widespread is the combining of regional representative offices and direct distributors network.

The strongest competition is observed for the right to sell the products in big supermarkets and shops, where exist widely accepted practice of paying for selling space.

Very interesting and promising is HOD market, which is developed only on 15-20% of its potential volume.

Ternopil region market overview.

There are about 300 mineral water sources on the territory of Ternopil region. The mineral water of 32 sources is included in the State Standard "Drinking mineral waters" and classified (according to the mineralization level): 12 – as table-medicinal and 20 – as table water.

In the 2005 there were about 24 companies producing the table-medicinal and table mineral water. Most of them are small producers oriented on the regional market. Two main operators on the market are Joint Ukrainian-Czech Company "Dobra Voda" (Zboriv district) and JSC "Brovar" (Mykulyntsi district). But their difference is producing the spring and not the mineral water.

Dynamics of mineral and spring water in the Ternopil region (Main Statistics Bureau in Ternopil region), thousand dal.

Period	Producing the mineral and spring water	Consumption of mineral and spring water
2003	464,5	498,7
2004	484,9	596,1
2005	490,3	671,6

After careful market research the company evaluated its potential strong and weak points and defined the most promising sections of the mineral water market:

- HOD (home and office delivery) which is at its starting point in the Ternopil region (developed only on 10% of its potential volume) and has a strong growing tendency.
- still mineral water market which is also developing (only in 2004 the demand for this type of mineral water increased on 41% (according to AS Nielsen data).

The main competitive advantages of “Ester” ltd would be:

- already existing wide distribution network (selling to the retail shops and chains, supermarkets)
- direct delivery to the customers (delivery to the companies and organizations offices, private households, catering companies etc)
- high quality combining with moderate price.

5. Marketing

Regarding the dynamic grows of mineral water market the marketing policy of “Ester” ltd would be based on the next directions:

- effective advertisement campaign targeting the widest circle of potential customers, creating the recognizable brand name and informing about its health improving effects;
- distribution through the existing sales network (selling to retail chains and shops, supermarkets etc)
- direct delivery to the customers (delivery to the companies and organizations offices, private households, restaurants, cafes etc)

The pricing policy would be based on establishing the equal price on still and sparkling mineral water for encouraging still water demand.

The average price for table mineral water in the region ranges as showed below:

- 0,5 liter bottle – 0,70-1,20 hryvnas (\$0,14-\$0,24)
- 1,5 liters bottle – 1,00-1,70 hryvnas (\$0,2- \$0,34)
- 5,0 liters bottle – 3,00-4,50 hryvnas (\$0,6-\$0,9).
- 15 liters container -15,00-20,00 hryvnas (\$3- \$4)

Regarding the planned net value and the profit rate (rate of return) the price for still and sparkling mineral water in PET-bottles produced by “Ester” ltd would be:

- 0,5 liter bottle – 0,75 hryvnas (\$0,15)
- 1,5 liters bottle – 1,20 hryvnas (\$0,24)
- 5,0 liters bottle – 3,30 hryvnas (\$0,65)
- 15 liters container -15 hryvnas (\$3).

The price of glass 0,33 liter bottle still and sparkling mineral water would be 1,20 gryvnas (\$0,23).

“Ester” ltd plans to carry out the next distribution scheme:

- HOD (Home and Office delivery) – 30% of output volume;
- retail network -30%
- catering organizations, hotels etc- 30%

- sanatoriums and spas -10%.

The main accent in the distribution policy would be made on establishing the long-term contacts with customers through allowing the discounts after signing the agreement about the permanent product delivery. Marketing policy would be based on the creating the well-known on the regional level brand “Kryshtaleva”, informing the potential customers about its unique health benefits and advertisement campaign, targeting the widest circle of potential customers.

6. Management and key persons.

The management of “Ester” ltd and the control of its economic activity is executed by its Director Maksymiv Petro Ivanovych who owns 60% of company’s own capital and Deputy Director Lypovets Volodymyr Stepanovych , who owns 40% of company’s own capital.

The organization structure of “Ester” ltd includes:

- administration department;
- marketing department;
- sales department
- procurement department.

7. Implementation planning.

“Ester” ltd plans the next project implementation schedule:

- October 2006- receiving the patent for using the brand “Kryshtaleva”
- February 2007- buying the PET-bottles production line, its installation and starting works
- March 2007 – buying the mineral water bottling line , its installation and starting works
- April 2007- active advertisement campaign, staff training and start of producing.
- May-August 2007 – gradual increase of output volume according to the demand.

8. Chances and risks.

There are next opportunities for the foreign partner

- creating the highly profitable company capable to keep the strong position on the regional mineral water market.
- entering the national market through the product range expanding and market growth.
- possibility of product export.

Risks:

Technological risk	Unsatisfactory quality of product or not reaching the planning production volume because of technological reasons	For covering this risk the company made a detailed research of main producers of PET-bottles production lines and mineral water bottling lines in Ukraine and abroad. After consideration its strong and weak points the choice was made in favor of German company “KXC” equipment and PET-bottles production line of “Sidel” company. It has a great reputation for its high quality and reliability. Those companies delivered their equipments for such big Ukrainian producers as “Obolon”, “Rosynka”, “Biola” (Dnipropetrovsk), “Slavutych” (Zaporizhya). After the production starts company plans to apply for certificate of international standards of quality ISO 9002
Marketing risk (customers behaviour)	Insufficient demand on the product, not reaching the planning sales volume	After careful market research the company evaluated its potential strong and weak points and defined the most promising sections of the mineral water market:

		<p>- HOD (home and office delivery) which is at its starting point in the Ternopil region (developed only on 10% of its potential volume) and has a strong growing tendency.</p> <p>- still mineral water market which is also developing (only in 2004 the demand for this type of mineral water increased on 41% (according to AS Nielsen data).</p> <p>The existing distribution network and carefully planned marketing strategy will cover this risk</p>
Competitive risk	Driving out from the market because of aggressive competitors campaign	The company has the significant competitive advantages and works for establishing the long-term contacts with customers through allowing the discounts after signing the agreement about the permanent product delivery. Those factors suppose to substantially reduce the competitive risk
Political risk	Legislation changes or unstable political situation which can put obstacles to the project implementation	<p>It is planned by government to make tougher requirement to the mineral water quality and introduce the new State Standard "Bottled mineral water. General technical conditions" and also to introduce the document about all drill sources passports requirements.</p> <p>But it won't influence the project implementation because of already proved high quality of mineral water, as shown in the certificate issued by Ukrainian SEI MRC of the Ministry of Health Protection in Odessa.</p>

9. Financial requirements.

The main financial characteristics of the project and the indicators of the economic efficiency are:

- total cost of the project – **\$ 643 000**, including: cost of already bought building and land - \$ 110 000, buying the PET-bottles production line- \$80 000, mineral water bottling line – \$ 448 000 (\$350 000 investor's financing and \$98 000 company's own recourses), equipment installation and starting work cost- \$5 000.
- amount of investment needed – **\$ 350 000**.
- planned production capacity – 3-3,5 million liters per year

Indicators	2007 (8 months)	2008	2009
1. Output volume, thousand liters	2 000	3 000	3 250
2. Sales volume, thousand \$	428,0	642,8	682,5
- sparkling mineral water PET	342,6	508,1	541,0
- still mineral water PET	43,2	69,5	72,5
- glass bottle water	42,2	65,2	69,0
3. Operating expenses	284,3	426,5	444,5
- material costs	86,6	129,9	140,7
- electricity, water costs	18,1	27,2	32,5
- staff wages	58,4	87,6	87,6
- depreciation expenses	39,6	59,4	58,8
- bank interest and fees	31,2	46,8	46,8

-others (transportation, advertisement etc)	50,4	75,6	78,1
4. Gross profit	143,7	198,3	238,0
5. Net profit	97,7	134,8	178,5

- net value of product 1 liter- 0, 70 gryvnas (**\$0,14**).
- product profitability-(net profit/ sales volume)*100% - **26,1 %** (after reaching full capacity)
- payback period – **28** months

The company's own capital in the total costs of project implementation is **54 %**.

10.Partner requirements.

“Ester” ltd is interested in the strategic partnership with the foreign investor which would be able to provide the \$350 000 investment needed for the implementation of this project.

The possible legal form of cooperation – the joint company establishment, equipment leasing, organization of joint production through the signing the agreement about joint activity etc.