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Russia's Growing Agricultural Imports

Causes and Outlook

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Approved by USDA's World Agricultural Outlook Board

Abstract

During the 2000s, Russian agricultural imports have grown considerably, from $7 billion in 2000 to $33 billion in 2008. This import growth has made Russia the second largest agricultural importer among emerging markets, after China. The main reasons for the import rise are macroeconomic—high growth in Russian gross domestic product, which increases consumer income and purchasing power, and real appreciation of the ruble, which makes imports less expensive vis-à-vis domestically produced goods. The economic crisis that hit Russia (and the world) in autumn 2008 makes the outlook for Russia's agricultural imports uncertain in the short term. However, the Russian economy is expected to stabilize within a year or two, at which time agricultural imports should continue to grow, although at a lower rate than in past years.

Keywords: Trade, imports, exports, U.S. agricultural trade, Russia, Russian agriculture, Russian agricultural trade, exchange rates

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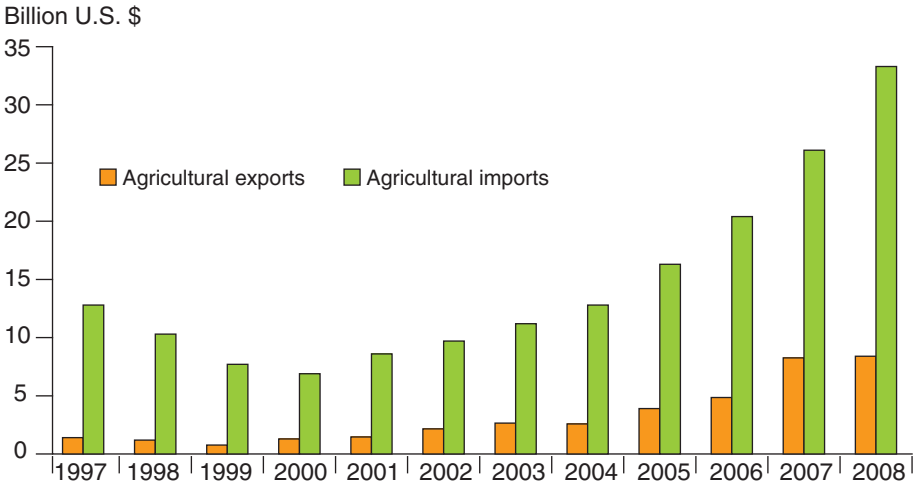
Introduction

The two main features of Russia's agricultural trade during this decade are that Russia is a big net importer and that imports have grown substantially (fig. 1). Between 2000 and 2008, agricultural imports increased from about $7 billion to $33 billion. The import growth has made Russia the second largest agricultural importer among emerging markets, after China. The main imports are meat, highly processed products, fruits, and vegetables (fig. 2). Russia's agricultural exports also grew during this time, although from a much lower base in value terms. Most of the export growth came from grain (mainly wheat and barley), such that, in 2007, Russia exported 16.6 million metric tons, worth $4.1 billion (fig. 3).

This report examines the reasons behind the surge in Russia's agricultural imports and the outlook for imports over the next few years. The main causes behind the import growth appear to be macroeconomic in nature, specifically high gross domestic product (GDP) growth, which increases consumer income and purchasing power, and real appreciation of the ruble, which makes imports less expensive vis-à-vis domestically produced goods. The key event that will affect Russia's agricultural imports in the short term is the country's financial and economic crisis that began in autumn 2008, which coincides with the world economic crisis. Although the crisis will negatively affect imports, the Russian economy is expected to stabilize within a year or two and resume growth. Agricultural imports then should continue to grow, although at a lower rate than in past years.

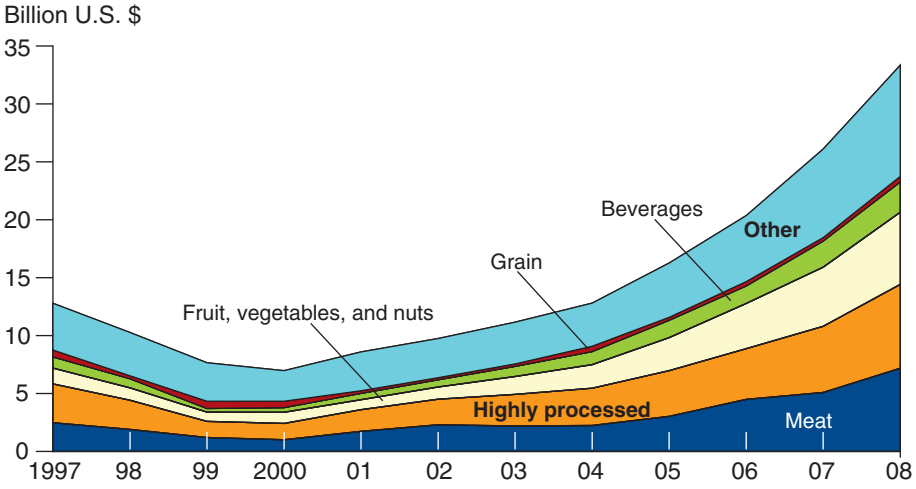
Figure 1
Russian agricultural imports have grown substantially since 2000



Source: World Trade Atlas, Global Trade Information Services.

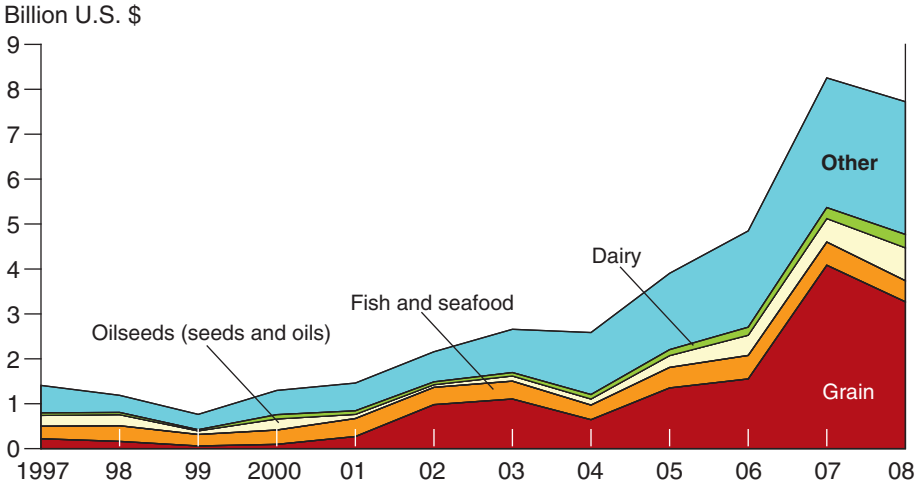
The U.S. share of Russia's agricultural imports in 2008 was a fairly small 6 percent, a drop from 10 percent in 2000 (World Trade Atlas). This decline is surprising, given that, between 2000 and 2008, the U.S. dollar depreciated substantially in real (inflation-adjusted) terms, not only against the ruble, but also against the euro and other currencies not pegged to the U.S. dollar, such as the British pound. The economic crisis that struck the United States in autumn 2008 and then spread throughout the world has strengthened the dollar against most other major currencies, as money flows into the United States as a "relatively" safe haven. The dollar appreciation has reversed some of the previous depreciation during the 2000s, making U.S. goods less price competitive in Russia compared with those from other exporting countries.

Figure 2
Russian agricultural imports, 1997-2008



Note: "Highly processed" exclude beverages and tobacco products.
Source: World Trade Atlas, Global Trade Information Services.

Figure 3
Grain has become Russia's top agricultural export



Source: World Trade Atlas, Global Trade Information Services.

Have Russian Agricultural Imports Increased in Volume as Well as Value?

Figures 1-3 measure trade in value, specifically in U.S. dollars, rather than volume. By 2008, meat made up about a fifth of Russia's agricultural import value. Table 1 shows that between 2000 and 2008, Russian meat imports (beef, pork, and poultry) also rose steadily in volume, from 1.81 million metric tons in 2000 to 3.43 million metric tons in 2008. Yet, meat import growth in volume was much less than in U.S. dollar terms (90 percent versus 570 percent).

The values in figures 1-3 overstate Russia's trade growth in volume, not only for meat but for all agricultural products, for two reasons. The first is that world agricultural prices have risen since 2000, surging in 2006-08 (fig. 4). The price growth has been highest for bulk crops, such as wheat and soybeans, and much less for meat and processed foods. Price growth for processed foods has been lower mainly because primary agricultural products typically account for a small share of their total value. For example, despite the large world price increase for grain in the 2000s, prices for grain-based processed foods (including baked goods) for U.S. urban consumers rose only 19 percent over 2000-2008 and 9 percent in 2006-08 (Bureau of Labor Statistics). During the 2000s, Russia has been a negligible importer of grain and oilseeds and a large importer of meat and processed foods, which means that the jump in world agricultural prices is a minor reason why the rise in Russia's agricultural import value overstates the rise in volume.

The second and more serious reason why trade values overstate volume growth is that the values are measured in U.S. dollars. During the 2000s, the dollar has depreciated substantially in real terms vis-à-vis the euro and various other major currencies. Between 2000 and 2008, the dollar fell in value against the euro by about a third, with the euro/dollar exchange rate dropping from 1.086 to 0.683 (ERS International Macroeconomic Data Set). The European Union (EU) countries as a bloc are the largest foreign agricultural supplier to Russia, followed by Brazil and the United States, which

Table 1
Russian meat production and imports, 2000-2008

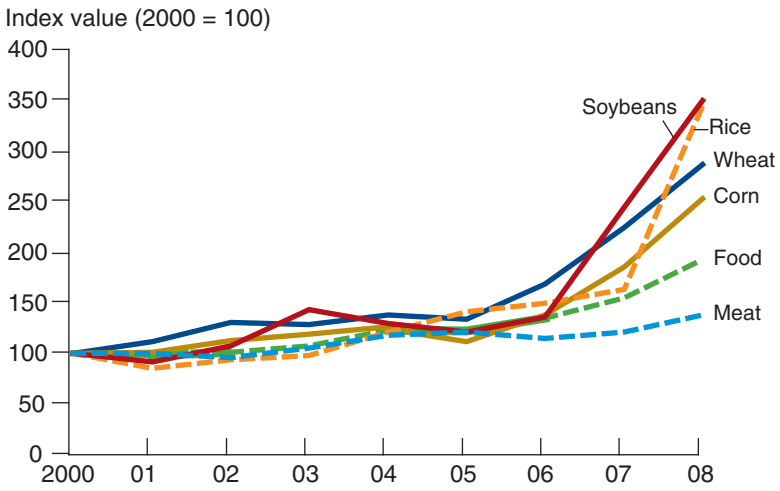
	Beef and veal			Pork			Poultry (broilers and turkey)		
		Imports			Imports			Imports	
Year	Production	Volume	Value	Production	Volume	Value	Production	Volume	Value
	--Million metric tons--		*$ Million U.S.*	*--Million metric tons--*		*$ Million U.S.*	*--Million metric tons--*		*$ Million U.S.*
2000	1.84	0.41	350	1.50	0.29	212	0.39	1.11	367
2001	1.76	0.64	511	1.56	0.49	322	0.44	1.45	750
2002	1.74	0.71	589	1.63	0.80	672	0.51	1.37	811
2003	1.67	0.71	616	1.71	0.71	651	0.57	1.20	696
2004	1.59	0.72	688	1.73	0.61	624	0.67	1.11	663
2005	1.53	0.98	954	1.74	0.75	819	0.92	1.33	848
2006	1.43	0.94	1,595	1.81	0.84	1,395	1.20	1.28	922
2007	1.37	1.03	1,770	1.91	0.89	1,637	1.38	1.30	1,052
2008	1.32	1.14	2,661	2.06	1.05	2,200	1.64	1.24	1,339

Source: Foreign Agricultural Service, Production, Supply and Distribution Online, http://www.fas.usda.gov/psdonline/; World Trade Atlas, Global Trade Information Services.

means that measuring Russian imports in U.S. dollars can severely overstate the magnitude in volume terms (fig. 5). If Russian agricultural imports are valued in euros rather than dollars, they rise from 7.4 billion euros in 2000 to 22.7 billion in 2008, an increase of over 200 percent compared with an increase of about 380 percent when the imports are measured in U.S. dollars.

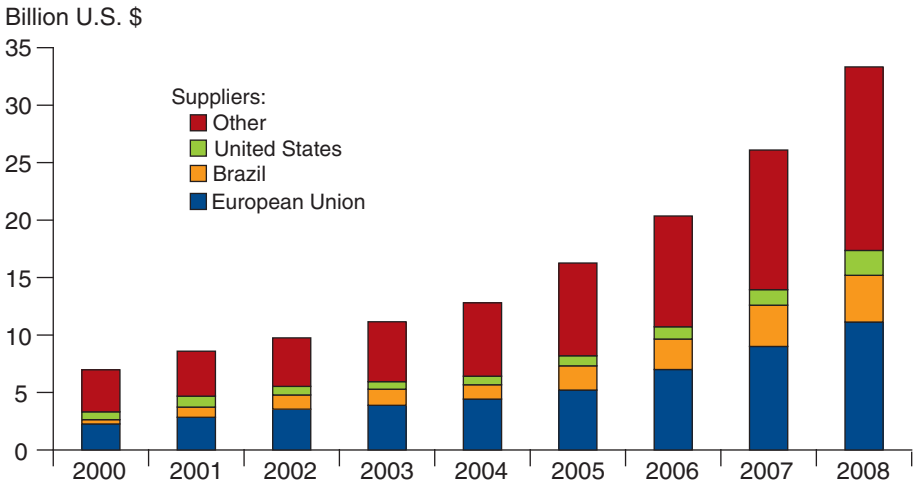
The dollar, however, has not depreciated as strongly against many countries' currencies as it has against the euro and has even appreciated against some. For example, Brazil has been Russia's second largest foreign agricultural supplier, and between 2000 and 2007, the U.S. dollar appreciated against the Brazilian real by 6 percent (ERS International Macroeconomic Data Set). For this reason, the growth in Russia's agricultural imports measured in euros

Figure 4
World agricultural prices surged in 2006-08



Source: Food and Agriculture Organization, Food Price Indices for meat, http://www.fao.org/worldfoodsituation/FoodPricesIndex/en/; International Monetary Fund, Primary Commodity Prices, http://www.imf.org/external/np/res/commod/index.asp.

Figure 5
U.S. is not a major agricultural supplier to Russia

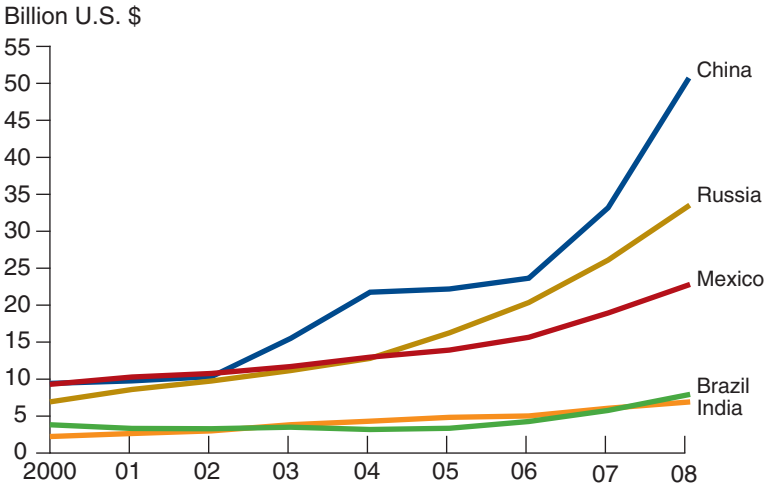


Source: World Trade Atlas, Global Trade Information Services.

can serve as a lower bound estimate of their growth in volume. Yet, even the increase of 200 percent in Russia's agricultural imports during 2000-2008 when measured in euros is considerable.

Figure 6 also supports the argument that Russian agricultural imports during the 2000s have grown in both value and volume. The figure shows that Russia's agricultural import value has grown faster than the import value of most other major non-Western countries. By 2008, Russia had become the second largest importer in the world among emerging market economies, after China. Given that all importing countries have been affected by recent world agricultural price inflation (although to varying degrees depending on their import commodity structure), Russia's import growth relative to that of other countries indicates growth in volume as well as value.

Figure 6
Agricultural imports by emerging markets, 2000-2008



Source: World Trade Atlas, Global Trade Information Services.

Why Have Russian Agricultural Imports Grown?

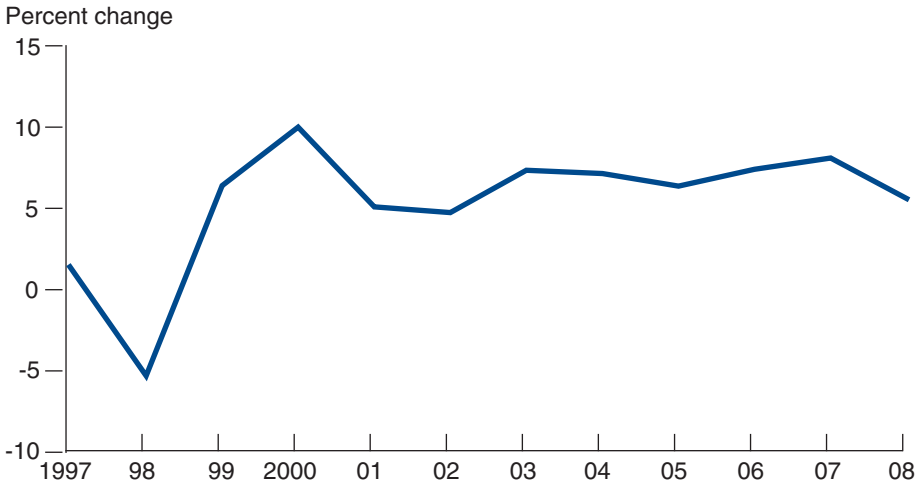
Russia's transition from a planned economy to a market economy, which began in the early 1990s, altered the structure of the country's agricultural production and trade. This report focuses not on the important systemic and policy changes of the 1990s that made growth in Russian agricultural imports possible in the 2000s, but rather on the economic reasons why imports rose so substantially during the current decade. The box, "Russia's Economic Transition and Commodity Agriculture," provides context for the report by examining how the major systemic and policy changes of the 1990s restructured Russian agricultural production and trade.

There are two main causes, both macroeconomic in nature, for the rise in Russia's agricultural imports during the 2000s. The first is high GDP growth, which over 2000-2008 averaged 7 percent per year (fig. 7). GDP growth increases consumer income and demand for food, although to the benefit of both foreign suppliers and domestic producers.

The second macroeconomic cause of rising agricultural imports is major real appreciation of the ruble vis-à-vis foreign currencies (fig. 8). Since Russia began its economic transition in 1992, the ruble has appreciated substantially in real terms. Part of the initial appreciation was a correction for major depreciation in 1991, the year the Soviet Union collapsed. Also, in the economic crisis years of 1998-99, the ruble depreciated sharply in both nominal and real terms, which helps explain why imports fell in those years (see fig. 1). Beginning in 1999, however, the ruble resumed its real appreciation, and by 2007, had risen to a value significantly above the 1997 pre-crisis level.

A change in the real value of a currency takes into account not only movement in the currency's nominal exchange rate, but also the difference in price inflation between the country in question and its trading partners. The real

Figure 7
High Russian GDP growth since 2000



Source: ERS International Macroeconomic Data Set, USDA, http://www.ers.usda.gov/data/macroeconomics/.

exchange rate thereby captures all the main variables that affect the price competitiveness of a country's domestically produced tradable goods vis-à-vis foreign products. The ruble has appreciated in real terms since 2000 mainly because relatively high inflation in Russia has exceeded the nominal depreciation of the ruble (and in fact, up to midsummer 2008, the ruble had also appreciated in nominal terms vis-à-vis the dollar and certain other currencies). The ruble's appreciation improved the price competitiveness of imports into Russia relative to domestic goods.

Russia's Economic Transition and Commodity Agriculture

Russia's transition from a planned to a market economy that began in the early 1990s fundamentally changed the structure of the country's agricultural production and trade. The country moved from being a heavy producer of livestock products and importer of grain and oilseeds to a major importer of livestock products and exporter of grain. These changes appear to have been an economically rational restructuring consistent with the country's underlying comparative advantage (and disadvantage) across major agricultural commodities (especially meat versus grain).

Around 1970, the Soviet Government decided to expand the livestock sector, the main motive being to raise consumers' standard of living by increasing meat and dairy consumption. Using large budget subsidies and controlled prices and trade, the regime succeeded in raising meat production by 63 percent between 1970 and 1990 (Liefert, 2001). Because the USSR could not produce enough animal feed to support the growing livestock herds, it became a large importer of feed grain, soybeans, and soybean meal, to the benefit of U.S. bulk crop producers.

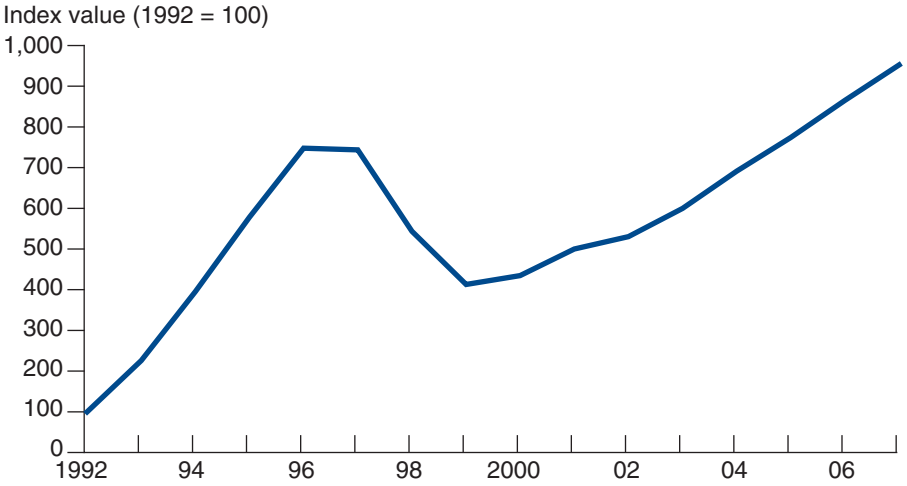
The move to a market economy in the 1990s reversed the expansion of the livestock sector during the planned period. Because of budget stringency, the huge government support to agriculture (and especially to the livestock sector, which received the bulk of subsidies) was largely eliminated. Also, integration into world markets revealed that Russia was a high-cost producer of livestock products; in other words, the country had a big comparative disadvantage in the sector (Liefert, 2002). Output of meat and other livestock goods plunged, and imports began to rise (Liefert, 2001; Liefert and Swinnen, 2002). Russian meat production in 2000 equaled 4.4 million metric tons compared with 10.1 million metric tons in 1990 (Rosstat).

During the 1990s, Russian consumers also were exposed to the array of world food products (as well as to other consumer goods) that they were denied during the planned period, which is another reason that the country's agricultural imports began to increase during the decade.

The severe downsizing of the livestock sector during transition considerably decreased the sector's demand for animal feed. Russian grain production fell, while imports of grain and oilseed products largely ended. During the 2000s, Russia has in fact become a major grain exporter, despite grain output in the decade being almost 20 percent lower than at the end of the Soviet period (Russian average annual grain output during 2001-08 was 83 million metric tons compared with 103 million tons during 1987-90 (FAS)). Rather than importing a lot of grain, soybeans, and soybean meal to support a large and inefficient livestock sector, Russia is now importing much more meat and other livestock products and exporting grain.

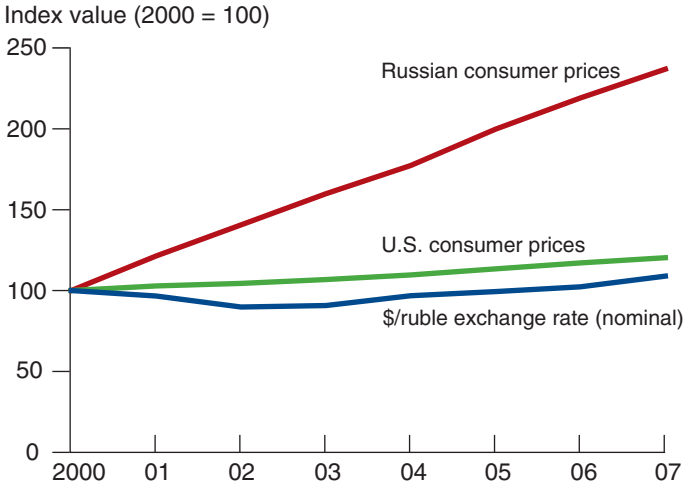
Figure 9 demonstrates this point by examining the change in the variables that determine the price competitiveness of imports from the United States (not just for agricultural products but all goods) vis-à-vis Russian domestic production. Since 2000, Russia has had average annual inflation of 13-14 percent, which over 2001-07 resulted in total inflation of about 140 percent. Also over this time, overall inflation in the United States was only 20 percent. Because of Russia's higher inflation, the real price of U.S. goods fell relative to Russian goods.

Figure 8
Russian real exchange rate, 1992-2007



Note: The exchange rate is measured in units of foreign currency per ruble (trade-weighted), such that a rise shows appreciation and a fall depreciation.
Source: ERS International Macroeconomic Data Set, USDA, http://www.ers.usda.gov/data/macroeconomics/.

Figure 9
Variables determining price competitiveness of imports from United States, 2000-2007



Source: Bureau of Labor Statistics, U.S. Dept. of Labor, Inflation and Consumer Spending, http://www.bls.gov; Rosstat, Russian Statistical Yearbook; ERS International Macroeconomic Data Set, USDA, http://www.ers.usda.gov/data/macroeconomics/.

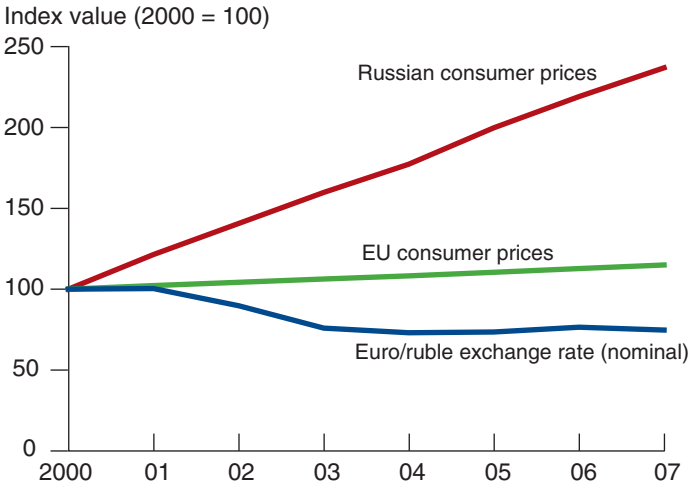
If a country has high inflation, its currency usually depreciates in nominal terms. The depreciation makes foreign currency more expensive in terms of domestic currency and thereby makes all foreign goods more expensive to the country's consumers. The currency depreciation corrects for the country's inflation by improving the price competitiveness of domestically produced goods vis-à-vis foreign goods. Figure 9 shows, however, that since 2000, the ruble has not depreciated nominally against the dollar to correct for Russia's much greater inflation than in the United States, and in fact, by 2007, the ruble was higher in value against the dollar than in 2000.

Figure 10 shows the change in the variables that determine the price competitiveness of imports from the EU relative to Russian production. Over 2001-07, the EU also had low overall inflation. The ruble did depreciate nominally over this time vis-à-vis the euro (unlike vis-à-vis the dollar), but not enough to correct for the substantial difference in inflation between Russia and the EU countries. This means that EU goods also increased in price competitiveness in Russia compared with domestic products, which boosted imports.

Figure 11 examines the effect of these macroeconomic developments on Russian food consumption from a somewhat different (though related) point of view. The figure shows the increase in the purchasing power of one unit of Russian labor time, say a day of work, vis-à-vis food from various sources; that is, it gives the increase in the volume of food that a typical Russian worker could buy with the wages earned from 1 day of his/her labor. The figure captures the effect on Russian food consumption from rising GDP and consumer income on the one hand and the real appreciation of the ruble on the other.

The wages and salaries of Russian workers increased so much that, by 2007, Russian labor could purchase about 160 percent more domestically produced food in volume than it could in 2000. Although food prices rose steadily

Figure 10
Variables determining price competitiveness of imports from EU, 2000-2007



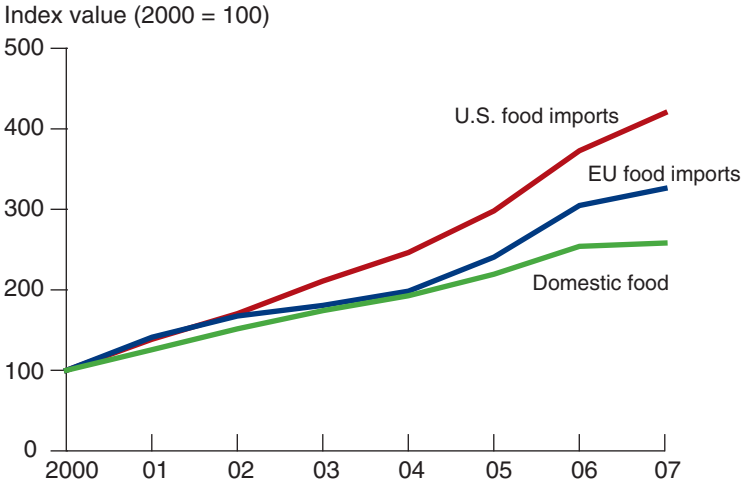
Source: Eurostat, Harmonized Indices of Consumer Prices; Rosstat, Russian Statistical Yearbook; ERS International Macroeconomic Data Set, USDA, http://www.ers.usda.gov/data/macroeconomics/.

over this period, nominal wages/salaries rose even more, such that consumer purchasing power increased.

However, by 2007, the purchasing power of Russian labor vis-à-vis food imports from the EU increased even more, by 225 percent, and vis-à-vis food imports from the United States, by 320 percent. Russian labor could buy more imported than domestic food because of real appreciation of the ruble—that is, because lower inflation in the United States, EU, and other trading partners compared with inflation in Russia made imports from those countries less expensive compared with domestically produced food. This appears to be the main reason why Russian agricultural imports have soared. Real appreciation of the ruble has helped Russian consumers by lowering prices for imports, but has hurt Russian producers who compete with imports.

Real appreciation of the ruble hurts not only import-competing Russian producers, but also those who export, by raising the prices that foreign buyers must pay for Russian products. Yet, Russian agricultural exports have also grown during the 2000s (see fig. 1). This growth, however, is from a small base of only $1.3 billion in 2000. Part of the growth in the dollar value of Russian exports is because of the dollar's depreciation during the 2000s. Also, as mentioned before, Russia's main agricultural export is grain, which has benefited from substantial growth in world prices since 2000. The price rise can increase the value of exports by raising both the unit value (price) and volume (through market supply response) of exports. Russia has also enjoyed favorable weather for grain production during the 2000s, with 2003 being the only bad year. Average annual grain production and exports during 2001-08 have been substantially above the levels of 1996-2000.

Figure 11
Purchasing power of Russian labor vis-à-vis food, 2000-2007



Source: Computed from data from Global Insight, Country Reports, Russia; Bureau of Labor Statistics, U.S. Dept. of Labor, Inflation and Consumer Spending, http://www.bls.gov; Eurostat, Harmonized Indices of Consumer Prices; Rosstat, Russian Statistical Yearbook.

What Role Has Policy Played in Import Growth?

Russian agricultural trade policy during the 2000s has allowed imports to grow by not being overly restrictive. Admittedly, the country's average agricultural import tariff rose from 10 percent in 2000 to 18 percent in early 2008. Yet, even 18 percent is not an especially high average tariff, given that the world average agricultural applied tariff in 2005 was 19 percent (calculated from the World Trade Organization), with many developing and developed countries having higher aggregate agricultural applied tariffs.

The main qualification to the above is that, as mentioned before, Russia is a big meat importer, and during the 2000s, the Government has taken strong measures to reduce meat imports. In 2003, Russia created tariff rate quotas (TRQs) for imports of beef and pork and a pure quota for poultry. The low in-quota tariff for beef and pork was kept at the previous tariff rate of 15 percent, while the out-of-quota tariffs were set at 60 and 80 percent, respectively. The tariff for quota poultry imports was maintained at the existing 25 percent. In 2005-06, the Government liberalized the meat import policy moderately by converting the pure quota for poultry to a TRQ and allowing the low tariff quota volumes for beef and pork to rise and the out-of-quota tariff rates to fall gradually over time. Yet, in January 2009, the Government made the TRQ regime more restrictive for poultry and pork. The low tariff quota volume for poultry was reduced from 1.252 to 0.952 million metric tons and the out-of-quota tariff rate was raised from 40 to 95 percent, whereas the out-of-quota tariff for pork was increased from 40 to 75 percent. The out-of-quota tariff for beef imports, however, was lowered to 30 percent (Interfax).

In the 2000s, the Russian Government has also strongly used health (sanitary) issues to ban or restrict meat imports from many countries, especially poultry from the United States. The controls are ad hoc and raise the concern among Russia's trading partners that the country is using sanitary issues as a protectionist pretext.

Despite the meat import TRQs and sanitary-based import restrictions, Russian meat imports have grown in both value and volume terms during the 2000s (table 1). Because of rising domestic demand for meat, Russia, by 2008, was importing beef, pork, and poultry at volumes above the quota levels assessed the low tariffs. Yet, without the TRQs and sanitary-based controls, Russian meat imports clearly would be higher.

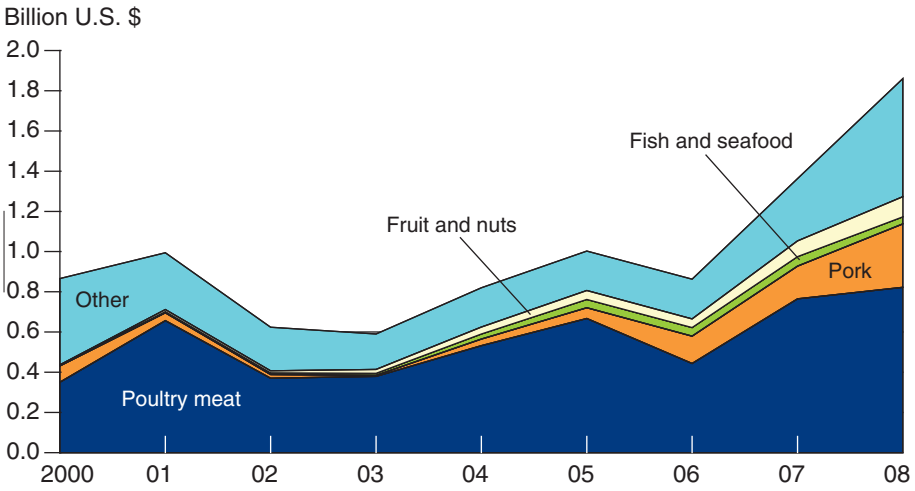
Why Is U.S. Share in Russia's Agricultural Imports So Low?

As mentioned earlier, the U.S. share in Russia's agricultural imports in 2008 was only 6 percent, down from 10 percent in 2000 (see fig. 5). This decline is puzzling, given that, during most of the 2000s, the dollar has depreciated substantially against the euro (by about a third during 2000-08) and other major currencies not pegged to the dollar, such as the British pound. This improvement in the price competitiveness of U.S. goods on world markets has increased overall U.S. agricultural exports (Gehlhar and Dohlman). However, the improvement in the price competitiveness of U.S. agricultural products in the Russian market compared with goods from the EU and

various other countries has not generated much of a rise in U.S. exports to Russia and no increase in market share. The only large U.S. agricultural export to Russia has been poultry, which in 2008, accounted for 44 percent of the value of U.S. exports to the country (fig. 12). Russia is the largest poultry importer in the world and the top foreign market for U.S. poultry, taking 20 percent of U.S. poultry exports in 2008 (World Trade Atlas).

Factors that might help explain the EU's top position in Russia's agricultural market, especially in contrast to that of the United States, are geographical proximity, early entry into the market at the beginning of the transition period in the 1990s, and greater familiarity with working in the country. European supermarkets and agro-food businesses developed long-term strategies for operating in Russia and invested accordingly. Nonetheless, U.S. producers apparently have not taken much advantage of Russia's large growth as a market for agricultural products, even with the benefit of a depreciating currency.

Figure 12
Poultry dominates U.S. agricultural exports to Russia, 2000-2008



Source: World Trade Atlas, Global Trade Information Services.

What Is the Outlook for Russia's Agricultural Imports in the Near to Medium Term?

The main factors and variables that will affect Russia's agricultural imports over the next few years are (1) GDP growth; (2) the ruble's real exchange rate; (3) world prices for agricultural commodities; (4) Russian agricultural output growth; and (5) Russian agricultural policies. Table 2 gives the likely status of these factors/variables in the near to medium term and the probable effect on imports.

The major event that will impact these variables is the financial and economic crisis that hit Russia in autumn 2008. Domestic causes of the crisis include concern that speculation had driven asset prices (especially stocks and property) to unsustainably high levels, worry about the overall strength of the financial system, and unease about the geopolitical consequences of Russia's intervention in Georgia. International-related causes are a contagion effect from the U.S. and Western financial crisis and the ensuing world economic downturn. In particular, the world recession has produced a plunge in prices for oil and natural gas, Russia's main exports. Because of the uncertainty involving both the Russian and world crises and their effects, projecting the direction and magnitude of change in the key factors and variables that will impact future Russian agricultural imports, especially in the short term, is challenging. The following predictions therefore are tentative.

Table 2
Effect of change in key variables on Russian agricultural imports

Variable	Expected future status	Expected effect on imports
GDP:		
Short term	Decrease	↓
Longer term	Moderate to high growth	↑
Real exchange rate	Change unlikely or direction uncertain	?
Inflation	Relatively high	↑
Nominal exchange rate	Change unlikely or direction uncertain	?
Trade balance	Surplus	↑
Capital flows	Outflows	↓
World agro-food prices	Change unlikely or direction uncertain	?
Domestic production	Increase for poultry and pork	↓
Policy		↓
Import tariffs	Change unlikely or direction uncertain	?
SPS-based import restrictions	Continue, and perhaps expand	↓
Subsidies	Increase	↓

GDP Growth

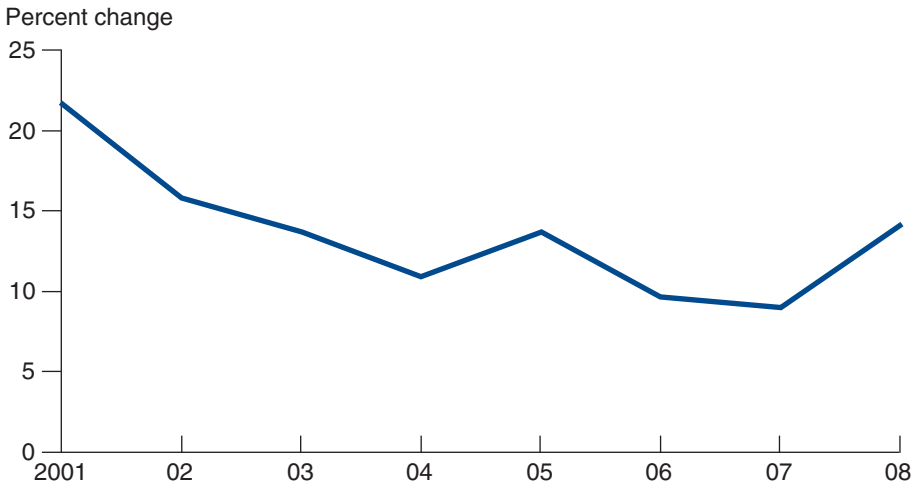
Before the economic crisis struck, macroeconomic forecasters were projecting continued high Russian annual GDP growth over 2009-12 of 5-7 percent. The crisis, however, will almost certainly cause GDP to fall in 2009 and perhaps in 2010. In April 2009, the macroeconomic forecasting firm Global Insight was predicting that 2009 Russian GDP would drop by 3.8 percent. The isolated effect of falling GDP and consumer income will be reduced agricultural imports.

If the economy stabilizes within a year or two, GDP soon could grow at 4-5 percent per year (as Global Insight is forecasting). Given that rising GDP would continue to increase consumer demand for food, especially for meat and other high-value products, the isolated effect of GDP growth would be to boost agricultural imports.

Real Exchange Rate of the Ruble

The change in the ruble's real exchange rate will depend on how high future price inflation is in Russia compared with that of its main trading partners, as well as change in the ruble's nominal exchange rate. Every year in the 2000s, Russia has had inflation of 9 percent or higher (fig. 13). Although inflation fell between 2001 and 2007, 2008 inflation jumped to 14 percent. Russia, therefore, likely will experience inflation of at least 6-10 percent a year during 2009-12 (Global Insight predicts average annual inflation of 11 percent). Between 2001 and 2008, average annual inflation in the United States and EU has been only 2-3 percent (Bureau of Labor Statistics; Eurostat). Because of the severe financial crisis that hit the United States and other major Western economies in autumn 2008, inflation in these countries in the near to medium term is not expected to be higher than inflation during 2001-08. Higher inflation in Russia compared with that in its main trading partners will continue to appreciate the ruble in real terms, making imports less expensive relative to Russian-produced goods. The isolated effect will be to increase imports.

Figure 13
Russian consumer price inflation, 2000-2008



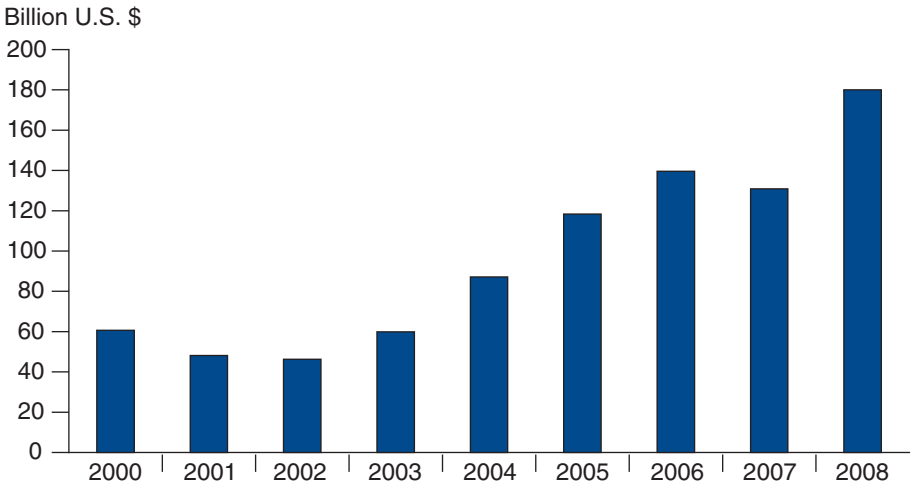
Source: Global Insight, Country Reports, Russia.

What is likely to happen to the ruble's nominal exchange rate? Nominal exchange rates are determined by both trade flows and capital flows. During the 2000s, Russia has had large overall trade surpluses (fig. 14). To put them in perspective, in 2005, Russia's trade surplus of $118 billion equaled 15 percent of GDP. During the 2000s, about two-thirds of Russia's export earnings have come from oil products and natural gas. The driving force behind the large growth in the trade surplus since 2002 has been the climb in world energy prices. In 2008, energy prices fell, with oil plunging from a peak of $147 per barrel in July 2008 (average daily price) to $32 per barrel at the beginning of 2009 (Energy Information Agency, 2008, 2009). Yet, world oil and natural gas prices during 2009-12 will probably remain above the low levels of 2000-2002, suggesting that Russia's trade surpluses will persist. Global Insight forecasts a 2009 trade surplus of $62 billion. The surpluses will strengthen the ruble because world demand to buy Russian goods with rubles will exceed Russia's demand to buy foreign goods with foreign currency. The isolated effect will be continued high demand for imported agricultural products.

High GDP growth and relative macroeconomic stability in Russia in the past few years helped motivate large foreign direct investment (FDI) in Russia, as well as investment in existing assets, such as stocks and property. For example, foreign investment in Russia in 2007 equaled $121 billion, including portfolio and direct investment (Rosstat). These capital inflows also helped strengthen the ruble. However, Russia's financial crisis has reversed these flows by triggering capital flight (especially by foreign investors), with net capital outflows in the fourth quarter of 2008 alone equaling $131 billion (World Bank, 2009).

The capital outflows have already substantially weakened the ruble, with the ruble/dollar exchange rate rising from 23.3 in mid-July 2008 to 33.1 by the end of April 2009 (Pacific Exchange Rate Service). However, the Russian Government appears committed to containing the financial crisis. The Government has injected substantial liquidity into the banking and financial system, as well as taken other steps to prevent any major banks or other key

Figure 14
Russian trade surplus, 2000-2008



Source: Global Insight, Country Reports, Russia.

financial intermediaries from going bankrupt. The Russian Central Bank has large foreign exchange reserves (earned by the country's trade surpluses) and the Government substantial savings (from previous fiscal surpluses) to support the economy financially. For these reasons, the Russian economy will likely stabilize within a year or two. Yet, the capital flight, which could continue in the near to medium term, has weakened (depreciated) the ruble, with the isolated effect of reducing agricultural imports.

Capital flows and their effect on the exchange rate are the main element of uncertainty in our outlook for Russia's agricultural imports. If capital flight is extreme, the ruble could continue to depreciate in nominal terms in the short to medium term despite the country's trade surplus. If the nominal depreciation of the ruble is so high that it exceeds the inflation differential between Russia and its major trading partners, the ruble could depreciate in real as well as nominal terms. Real depreciation would make imports more rather than less expensive vis-à-vis domestic production, thereby reducing agricultural imports.

World Agricultural Prices

Another factor that could affect Russia's agricultural imports is world agricultural prices. Russia was hit by the 2006-08 jump in prices, with food prices rising by more than overall inflation. Distributional effects of the price growth are that higher prices hurt Russian food consumers but should have helped agricultural producers—the reverse of the effects of real appreciation of the ruble.

Price growth for a country's imports can affect the value of the imports in two ways. It can, first, reduce physical import volume but, second, increase import unit value, which means that the net effect on the total value of imports will be unclear and depend on how sensitive import demand is to price changes. If demand is sensitive to price changes, or price elastic, the drop in import volume will dominate the price increase, such that the total value of imports will fall. If demand is insensitive to price changes, or price inelastic, the price increase will dominate the decline in import volume, such that the total value of imports will rise. The net result will vary by commodity, and not enough time has elapsed since the recent price surge for sufficient data to exist to answer this question clearly for Russia's specific agricultural imports.

More importantly, though, is that the recent jump in world prices peaked in early to mid 2008 and prices have since fallen. For example, world wheat prices, at a high in March 2008, fell by 50 percent by December 2008, while soybean prices dropped by 42 percent between July and December 2008 (IMF Primary Commodity Prices). One reason for the price decline is that the earlier high prices motivated significant world supply response in 2008, especially for bulk crops. Thus, world agricultural prices will not necessarily rise over the next 5 or so years, although they could settle at higher values than those during 2001-05. For Russia, this means that in the near to medium future, world prices probably will not be a key factor in changing agricultural imports compared with the 2006-08 import value and volume.

Agricultural Production

From 2000 to 2008, Russian agricultural production grew by about 38 percent (Rosstat). Total meat output also rose, although performance varied by product (see table 1). Poultry production increased by 322 percent (although from a small base) and pork by 37 percent, whereas beef fell 29 percent. Agricultural output growth during the 2000s in particular compares favorably with the huge drop in production during the 1990s (see Liefert and Swinnen, 2002).

One likely reason for overall agricultural output growth is the rise during the 2000s of new types of agricultural "operators," which typically are large vertically integrated enterprises that bring advanced technology, superior managerial expertise, and investment into the sector (Serova, 2007; Rylko et al., 2008). These new operations are an improvement over the moribund former state and collective farms that have been the dominant type of agricultural producer in the transition period. Development of large modern enterprises is one reason poultry production in particular has boomed, which in turn, has resulted in much less growth in Russian poultry imports during the 2000s than in beef and pork. Beef output, on the other hand, continues its inexorable fall because Russia has not developed a modern beef-producing industry, with most production coming from the slaughter of old dairy cattle.

In general, Russian agriculture continues to perform far below its potential, with weaknesses in management, work incentives, adoption of new technology, and market linkages (see Lerman, 2008). The sector still suffers from a surplus of elderly workers and a shortage of skilled specialists, such as in machinery use and repair, animal care, and management. Improvement in these areas would increase productivity and output. Building on the already modest progress of this decade, production should continue to grow over the next 4-5 years, with the isolated effect of reducing imports.

Agricultural Policy

The last major factor that will affect Russia's future agricultural imports is government policy involving production and trade. In 2005, the Russian Government designated health, education, housing, and agriculture as national priorities that would receive increased funding. From 2005 to 2007, total state support to agriculture (from both the Federal and regional governments) rose 87 percent in nominal rubles and 52 percent in real (2005 constant) rubles (Rosstat). The Government has stated that the main goal of agricultural policy and increased support is to expand the livestock sector, given its large contraction during the transition period.

Statements by the Russian Ministry of Agriculture and the Government in general indicate a strong desire to reduce agricultural imports, especially of meat (Interfax). Growing state support to agriculture and continued use of sanitary-based import bans and restrictions could help achieve that goal. A potential constraint on Russia's ability to reduce imports through state policy would be accession to the World Trade Organization (WTO). Russia officially began its WTO accession bid in 1995 (and to the General Agreement on Tariffs and Trade in 1993), and by mid-2008, had concluded bilateral negotiations with almost all countries (including the United States and EU).

The three pillars of the Uruguay Round Agreement on Agriculture are market access, export subsidies, and domestic support. With respect to all three pillars, Russia has been asking for bound commitments above the current levels. As mentioned before, Russia's current average agricultural import tariff is about 18 percent, up from 10 percent in 2000. However, throughout its accession negotiations, Russia has been asking for bound agricultural tariffs above actual applied tariffs. Although Russia has not used any agricultural export subsidies during the transition period, and such subsidies have been targeted for elimination within the current Doha Development Round of trade negotiations, Russia has been requesting annual bound export subsidies of $0.7 billion. On domestic support, Russia is asking for annual bound support of $9.5 billion, which compares with its 2007 actual support level of $5.7 billion (Russia and World Trade Organization website; Rosstat).

In August 2008, the Russian Government announced that it was withdrawing from certain agreements made as part of its WTO accession negotiations and that the country had little to gain from WTO membership. Russia has since renewed its WTO accession negotiations. Yet, as mentioned before, in December 2008, the country made its tariff rate quota regime for poultry and pork imports more restrictive, mainly by raising the higher out-of-quota tariffs.

If Russia soon joins the WTO, it is unclear what its bound level of tariffs and support would be, perhaps above current levels as the Russians have been negotiating. Accession on such terms would not liberalize Russian agricultural trade and support policies and, thereby, would not increase imports, but it would benefit U.S. and other foreign suppliers in the long term by providing a cap on the rise in tariffs and support. The main gain to Russia's agricultural trading partners from the country's WTO accession might be that it would give them an official forum for challenging Russia's sanitary and phytosanitary import restrictions.

Conclusion

Of the main factors/variables that will affect Russia's future agricultural imports, four should continue to develop in the near term in ways that reduce imports—falling GDP, capital outflows, increasing domestic agricultural production, and changing policy. On the other hand, domestic inflation and the country's overall trade balance (surplus) will probably develop in directions that promote imports. The likely renewal of GDP growth in a couple of years would strengthen the import-expanding forces. Capital flows and policy are variables of major uncertainty in terms of both course and magnitude. Because of this uncertainty, forecasting the path of Russia's agricultural imports is especially difficult. Yet, as the Russian economy stabilizes and growth resumes, Russian agricultural imports will probably resume growth, although at a lower rate than in past years.

The U.S. share in Russia's agricultural imports in 2008 was fairly small at only 6 percent, a drop from 10 percent in 2000. This outcome occurred despite the depreciation of the dollar against the euro and other currencies not pegged to the dollar over most of the earlier 2000s, which increased the price competitiveness of U.S. agricultural products vis-à-vis goods priced in the currencies of these countries. The appreciation of the dollar since autumn 2008 has negated some of the improvement in price competitiveness for U.S. agricultural goods gained during previous years. Yet, the likely resumption in the growth of Russian imports in a couple of years could provide U.S. exporters with a new opportunity to expand market share in the country that has become the world's second largest agricultural importer among emerging markets.

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