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The review provides a detailed analysis of main trends in Russia's economy in 2013. The paper contains 6 big sections that highlight single aspects of Russia's economic development: the socio-political context; the monetary and credit spheres; financial sphere; the real sector; social sphere; institutional challenges. The paper employs a huge mass of statistical data that forms the basis of original computation and numerous charts.

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## **Russian Agriculture: the First Year within the World Trade Organization**

### General outline of agricultural performance

On the eve of Russia's accession to WTO the debate held in the country about possible adverse effects of this step grew more fierce. The main hazard for Russian farm producers was considered to be the commitment to reduce import duties: from the moment of accession the average maximum duties on agricultural items were to be cut from 13.2% to 10.8%<sup>1</sup>. The system applied in Russia prior to entering WTO envisaged support to agriculture primarily by means of transfers from final consumers who paid higher prices (as compared with the world ones) for most farm products. The lowering of duties and consumer transfers implies an actual curtailment of aggregate support to domestic producers. The reduction of risks and preservation of the existing level of aggregate support to Russian farm producers would require an increase of their budget support. But such policies would be in disaccord with the current budget capabilities and potentially would contradict the terms of the country's accession to WTO restricting amber box<sup>2</sup> protection measures.

Formally, at the federal level Russia applies long-term mechanisms of state support to farm producers – the financing should comply with the guidelines and amounts envisaged by a regular State program for agricultural development and regulation of agricultural, input and food markets (hereinafter – the State Program) in effect within a particular period (2008-2012, 2013-2020). But in 2013 the mechanisms of support were altered as regards both volumes and directions. In particular, selected sectors still got additional support in excess of the limits stipulated in the State Program<sup>3</sup>. The allotment of extra budget funds was not directly linked to the WTO accession but was substantiated by the worsening performance of selected sectors following the accession and by the unfavourable conditions of 2012.

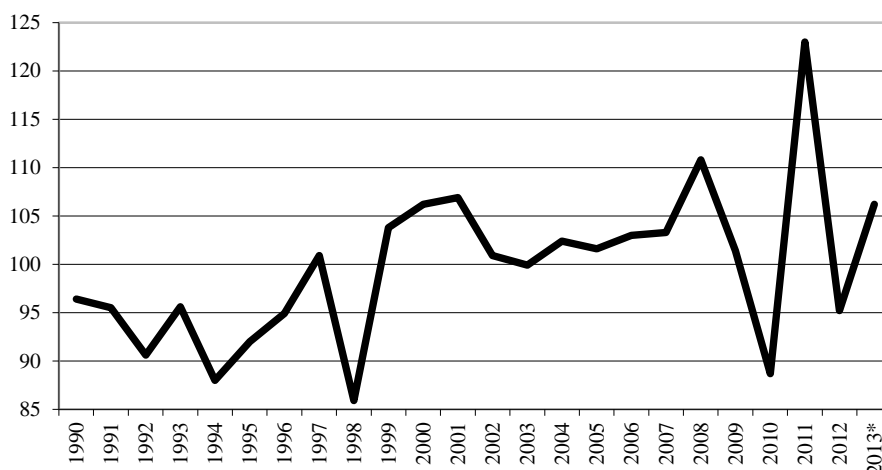
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<sup>1</sup> Tariff rates for meat products (beef, pork, poultry meat) differ depending on whether the deliveries fall within the quota or are made out of quota. Within the quota the tariff rate for beef is 15%, in excess of it – 55% (for pork – 0% and 65%, respectively). A matter of concern was the abolition of customs duty on import of live pigs. The lowering of specific duties is to be enacted at different dates – some of them come into force at once, others – within the period from 2 to 8 years after the moment of Russia's accession to WTO.

<sup>2</sup> Traditional measures of support applied in Russia are mostly those regarded as so called amber box tools. See: Shagayda N.I. *Otsenka byudzhetykh raskhodov i byudzhetnoy podderzhki v sel'skom khozyaystve Rossii* [Estimate of budget expenditures and budget support in Russian agriculture] // *APK: ekonomika, upravleniye* [Agro-industrial complex: economy, management]. No. 12, 2012, pp. 14-22.

<sup>3</sup> In 2013 the financing envisaged by the State Program was increased by nearly 30%. A part of additional funds was allocated to the reimbursement of expenditures of pig, poultry and egg producers on the purchase of feeds, the prices for which grew due to the unfavourable weather conditions in 2012.

Judging by production indicators, 2013 was a better year for agriculture as compared with 2012: its gross output exceeded that of 2012 by 6.2% (Fig. 44). But this was due not to a sustainable trend but to poor indicators of the previous year against which the 2013 performance looked better.



\* - 10 months.  
Source: Rosstat.

Fig. 44. Index of agricultural production in all types of farms (in comparable prices, as % of the previous year)

As compared with 2012, the output of grain in 2013 increased by 30%, the output of sunflower seeds – by 11%. The production of sugar beets that used to develop quite dynamically, in 2013 notably fell – by 18% (Table 36). The cause of this decrease is to be sought in the change of prices for sugar and the consequent lowering of potential incomes from production of sugar beets resulting in the reorientation of producers towards growing of grains and oilseeds that were more lucrative that year. Grain crops and sunflower seeds compete with sugar beets for areas in the main regions producing this crop.

Table 36

**Gross output of basic farm crops in farms of all types, 1,000 tons (annual average)**

	1990–1995	1996–2000	2001–2005	2006–2010	2011–2013	For reference:	
						2012	2013*
Grains and legumes	92737	65097	78832	85190	85483	70908	91329
Flax fiber	72	38	53	45	64	46	38
Sugar beets	23440	14023	18530	27130	43482	45057	37747
Sunflower seeds	3158	3330	4507	6313	9298	7993	10204
Potatoes	35798	31834	28359	27315	30801	29533	30189

\* - preliminary data.  
Source: Rosstat.

Table 37 shows the production dynamics for basic livestock products in corporate farms<sup>1</sup>. In 2013 the process of putting in operation large pig and poultry complexes went on resulting in the increase of overall production of meat despite the continuing decline of beef production

<sup>1</sup> The data for all types of farms is not available.

in corporate farms. The increase of pork output exceeded 15%, that of poultry meat was about 10%. The most part of these products are produced in corporate farms (*Fig. 45*).

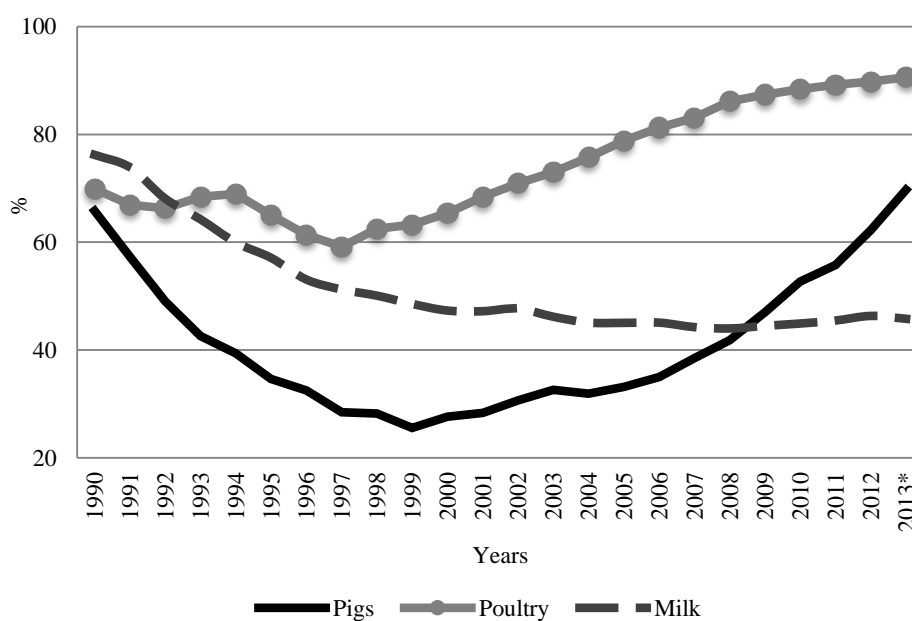
Table 37

**Production of basic livestock products in corporate farms,  
1,000 tons (annual average)**

	1990–1995	1996–2000	2001–2005	2006–2010	2011–2013	For reference:	
						2012	2013*
Slaughter livestock and poultry (slaughter weight)	5087	1994	2112	3428	5392	5415	6002
including:							
Cattle	2638	1049	761	592	528	533	538
Pigs	1332	447	510	888	1652	1594	2007
Sheep and goats	143	30	15	15	17	17	17
Poultry	925	440	809	1917	3192	3255	3463
Milk	31758	16825	15051	14270	14398	14752	14048
Eggs (million pieces)	30782	22858	26307	29307	32286	32768	32241

\* - preliminary data.

Source: Rosstat.



\*- preliminary data.

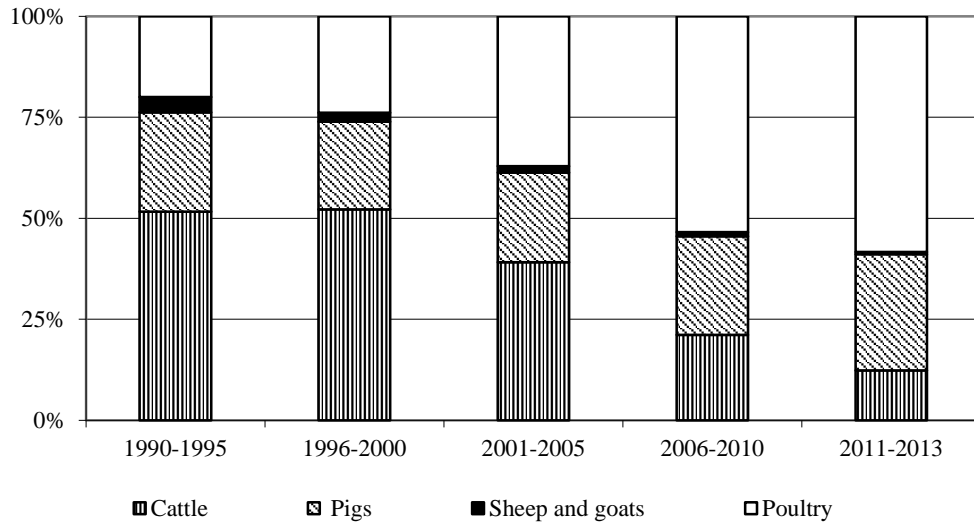
Source: Rosstat.

*Fig. 45. Share of corporate farms in production of basic livestock products as % of the aggregate output*

In spite of all the efforts of state to stimulate production of milk, in 2013 its output was down 4.7% as compared with 2012. A sharp increase of pork and poultry meat output in corporate farms resulted in a noticeable shift in meat production structure (*Fig. 46*).

Production of pigs continues to concentrate in corporate farms due to the forced reduction of their population in household farms (attributed to the risk of disease spread in case of home

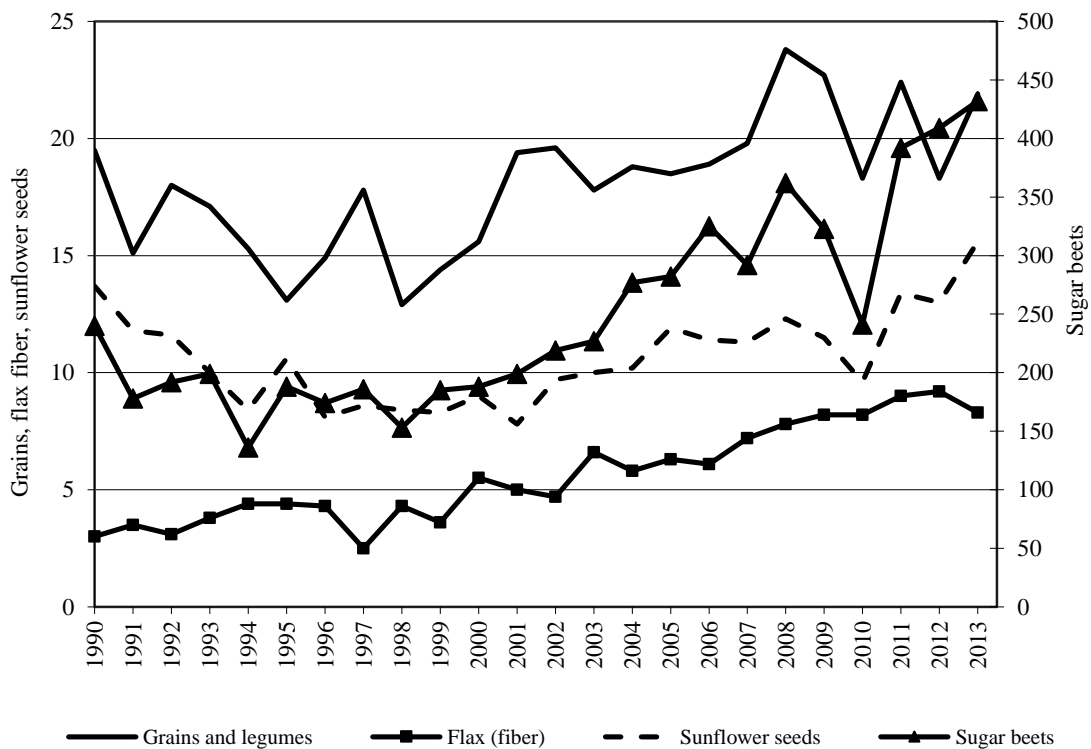
raising of livestock). However, it affects the financial performance of rural households that still keep over 20% of the total pig inventories (in 2006 – over 50%).



Source: Rosstat.

Fig. 46. Structure of meat production by types of livestock, %

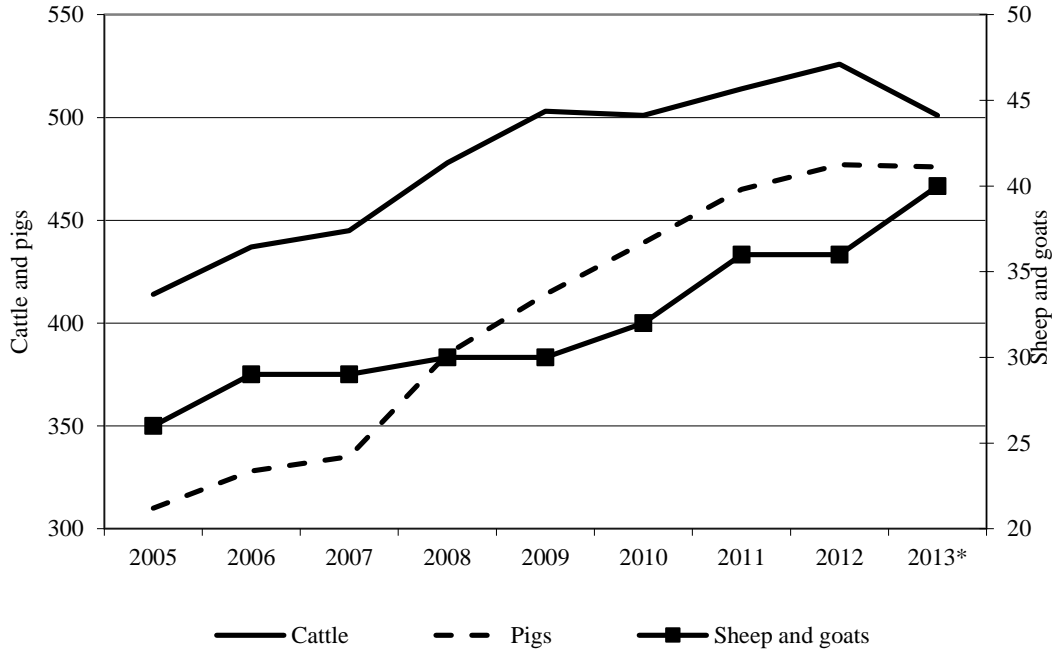
In crop production the yields of all basic farm crops continue growing (Fig. 47).



Source: Rosstat.

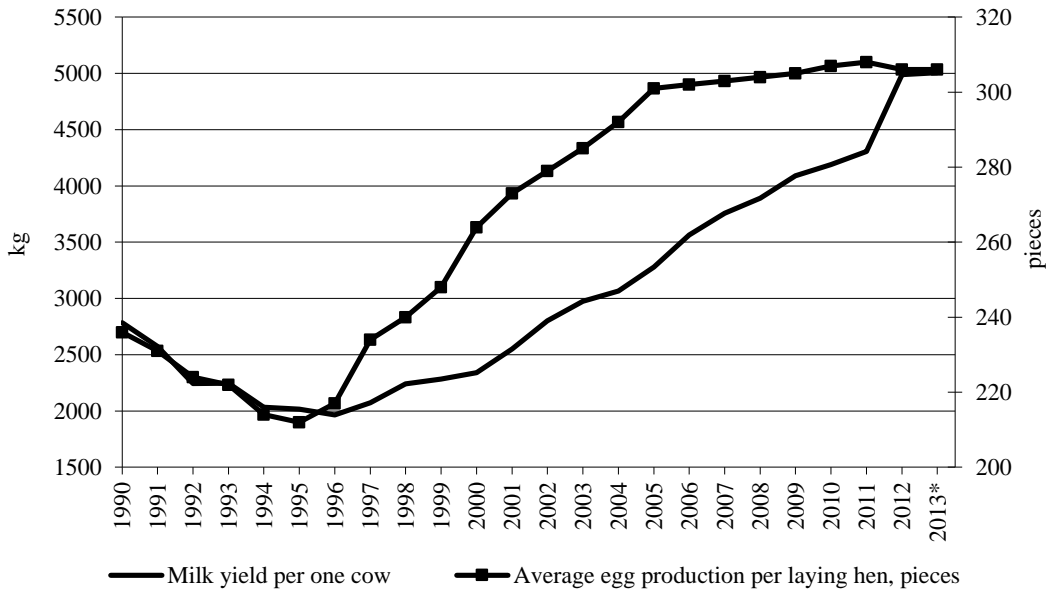
Fig. 47. Yields of basic farm crops, centners per hectare

In livestock production higher average daily weight gains in 2013 were recorded only in the raising of sheep while for pigs they remained at the 2012 level and for feeder cattle even dropped. The productivity of milk cattle raising and production of eggs did not change (Fig. 48 and 49).



\* - January-September.

Fig. 48. Annual dynamics of average daily weight gains of livestock in corporate farms (grams)





\* - 2013 - estimate.

*Fig. 49. Productivity of livestock and poultry  
in corporate farms*

Labour productivity in agriculture continues to demonstrate an upward trend. By the beginning of 2013 in corporate farms it was more than 4 times higher than in 1990<sup>1</sup>.

*Situation on selected agricultural and food markets*

2013 was the first year of Russian agricultural and food markets' operation within WTO. Among the main concerns associated with conditions of joining this world organization were the risks of domestic production decline, growth of imports and the respective weakening of national food security. Indeed, last year the situation in some agricultural sub-sectors was really difficult. But it was not so much due to the fulfillment of Russia's commitments to reduce import tariffs after joining WTO as to a whole range of other conjoint negative factors: the growth of prices for formula feeds in livestock production, the positive world price dynamics on some commodity markets, Russia's accession to the Customs union.

Imports of agricultural and food products after the country's accession to WTO did not change much. According to data of the RF Federal Customs Service, within 10 months 2012 the value of imports fell by 5.3% against the respective period of 2011 and in 2013 it grew by 4.1% against the respective period of 2012<sup>2</sup>.

A matter of concern on the eve of accession to WTO was the probable growth of meat imports. However, imports of red meat fell by 11.7%, imports of poultry meat – by 6.2%. Imports of shellfish increased by 21.3%. Imports of butter and other milk fats grew by 16.1% while imports of dried milk – by more than 48% which is a disturbing rate. Coupled with larger imports of palm oil (up 27.8%) this can be an indirect evidence of softening control over compliance with technical regulations for milk and dairy products or of quite legal increase of foodstuffs' production out of reconstituted milk.

On the contrary, the value of Russia's exports of agricultural and food products in 10 months 2013 fell by 9.4%. It was due to the reduction of export supplies of wheat (by 26.5%), sunflower oil (by 22.7%) and wheat flower (by 44.9%). At the same time the specific trend of the past year was the penetration of Russian meat products to foreign export markets (still, the volumes exported in 2013 remained quite modest – they totaled about 50,000 tons for both meat and sub-products). The major importers of meat from Russia are countries of Middle and South-East Asia (China, Kazakhstan, etc.). The main items exported to foreign markets are poultry meat, pork sub-products and finished meat products.

In Russia the excess of domestic food prices over the world ones (that forms primarily due to the application of import duties and quotas) is the basic mechanism of support to farm producers. Producers of meat and milk enjoy the biggest price support. After Russia's accession to WTO import duties on pig sector's produce noticeably fell: the tariff on import of pork within the quota reduced from 15% to zero, on its import above the quota – from 75% to 65%. The tariff on import of live pigs plummeted several fold – from 40 to 5%. Other food items were

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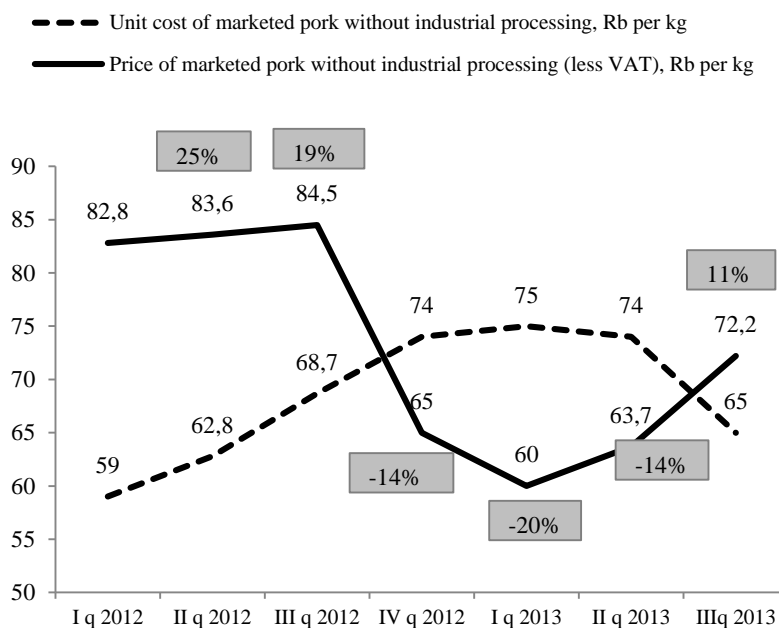
<sup>1</sup> Uzun V.Ya. *Rezultaty yeltsinskoy agrarnoy reformy*. [Results of Yeltsin's agrarian reform] // *Ekonomika sel'skohozyaystvennykh i pererabatyvayushchikh predpriyatiy*. [Economics of agricultural and processing enterprises]. No.4, 2013, pp. 19-26.

<sup>2</sup> Hereinafter the data relates to imports and exports in 10 months 2013 and includes trade with the Republic of Belarus and the Republic of Kazakhstan.

not subject to such dramatic liberalization of import restrictions in the first year of Russia's membership in WTO. According to commitments undertaken by our country the lowering of import duties is to proceed gradually – within the so called implementation period. For most agricultural and food items this period ends in 2015-2016.

In the first half of 2013 the domestic meat sector was affected by the growth of imports and the combination of record high prices for feeds with low purchase prices for basic types of meat. As a result its profitability fell. In the second half of the year the situation in meat sector improved owing to lower cost of feeds for livestock production.

The fourth quarter of 2012 – the first quarter of 2013 were a period of severe crisis in pig raising. Within this period negative trends in the sector were conditioned by a temporary growth of pork imports due to the lowering of import tariffs in the framework of Russia's commitments to WTO, higher prices for grain and the oversaturation of the market owing to both the increase of domestic output of pork in corporate farms and larger import supplies. As a result prices for live pigs in corporate farms fell by 25-30%<sup>1</sup>. All these factors led to the drop of profitability in pig raising (Fig. 50). Negative and even zero margins in the period when the sector was undergoing an active phase of investment development can affect the growth prospects of industrial pig production after 2014 if the ratchet effect of increase preserves in 2013-2014. In its turn, the danger of further spreading of ASF<sup>2</sup> and the above mentioned growth of prices for feeds contributed to the cut of livestock inventories in household farms. As a result, there appeared risks of a sharp production drop in the Russian pig sector and the return to situation observed five years ago when the share of imports on the market reached 40-50%.



Source: National Union of Pig Producers.

Fig. 50. Profitability of pig raising in the Russian Federation in 2012–2013

The risk of disease spread and the detected cases of violation of veterinary and sanitary requirements as to the use of ractopamine (feed supplement for increasing muscle mass of pigs

<sup>1</sup> According to data of the National Union of Pig Producers.

<sup>2</sup> African swine fever.

and cattle) and antibiotics forced Russia to introduce restrictions on import of live pigs and pork from the countries of EU, North, South and Latin America and the Republic of Belarus. Together with the removal of pork and poultry meat from the list of goods the import of which from developing and least developed countries is eligible for tariff preferences, eased pressure on domestic pork production. Import supplies of pork started to fall already at the beginning of 2013. Coupled with the lowering of domestic prices for grain, this supported the growth of prices for pork in 2013 and helped domestic pig producers to achieve a positive profitability rate of 11% in the third quarter of 2013.

On the whole, despite all the problems faced at the beginning of 2013, the market of pork demonstrated record annual rates of domestic production growth and a shrinkage of imports. For instance, in 2013 the output of pork in corporate farms grew from 1,594 thousand tons to 2,007 thousand tons slaughter weight (up 25% *Table 37*). Meantime, the decrease of livestock population and production in household farms accelerated. In the situation of tougher competition with imported products non-efficient producers quit the market. Despite the positive dynamics in domestic pig raising sector, the share of imports in the total pork market capacity remains relatively high – about 29%<sup>1</sup>.

The situation on the market of poultry meat was similar. The lowering of prices for poultry conditioned by high saturation of the domestic market and larger cost of formula feeds affected the profitability of poultry plants – the respective sector's average fell down to 5%<sup>2</sup>. Still, production of poultry meat continues to grow by inertia while imports are slightly shrinking. After a boost in 2010-2012 the sector's growth rates somewhat declined but nevertheless remain rather high. In 2013 the annual output of poultry in corporate farms increased by 6.3% and reached 3,463 thousand tons slaughter weight (*Table 37*).

The domestic market of poultry meat is close to saturation. The share of imports thereon fell down to 13%. But as different from pig raising where the growth of industrial production offsets the decline of output in household farms, in poultry breeding such substitution is impossible – about 90% of poultry meat is produced by the industrial poultry plants. Therefore, further growth of the domestic poultry production is feasible only in case of developing export supplies. Taking into account specifics of pricing different broiler parts, domestic poultry meat has a good export potential.

The production of beef didn't feel any direct effect of accession to WTO as almost all beef in the country is a by-product of milk cattle breeding. The crisis of milk industry fostered a decline of cattle herd. At the same time positive structural shifts are taking shape in the sector inter alia owing to the active state support – the population of meat breeds and mixed bred cattle is increasing. According to the data of IKAR, in 2013 the rate of increase of meat cow number (22%) exceeded that of the cattle herd in general.

In 2013 the output of slaughter cattle meat in corporate farms didn't fall for the first time in many years – 538 thousand tons against 533 thousand tons in 2012 (*Table 37*). It should be noted that the demand for beef is limited by its relatively high price as compared with that for pork and poultry meat. That's why the growing supply of the latter will continue to force beef out of retailing and processing. Consequently, in the medium term the development of domestic cattle meat sector will result in increased production of quality beef rather than in bigger total output of this kind of meat.

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<sup>1</sup> According to data of IKAR.

<sup>2</sup> According to data of IKAR.

As mentioned above, in 2013 the situation in milk sector that in recent years was stagnant became even worse: the output of raw milk fell and imports of dairy products increased. However, this aggravation was not due to the Russia's accession to WTO but was rather conditioned by problems of domestic origin.

The output of milk in corporate farms fell by more than 700 thousand tons and that in all categories of farms – by 1.5 million tons as compared with 2012. The reduction of raw milk output in Russia is due to the shrinkage of milk cattle inventories and productivity resulting from poor quality of rough feeds and the rise of prices for formula feeds.

The drop in production of raw milk has toughened competition of processors for this input and led to the increase of purchase prices for milk. According to data of the RF Ministry of Agriculture, the average price received by domestic producers of raw milk grew from Rb 15.6 per kg at the beginning of the year up to Rb 17.9 kg per kg by mid-December 2013 (up 14.4% as compared with the respective date of 2012).

In the situation of continuing deficit of raw milk and high purchase prices for this input one could observe a substitution of some dairy products for other – the production of items requiring much milk (such as cheese and dried milk) was falling while that of whole milk products (kefir, yoghurt, cream) was growing (*Table 38*). High prices for milk inputs on the domestic market coupled with positive dynamics of the world prices for dried milk following the drought in New Zealand fostered the growth of prices for finished dairy products in Russia. During the year average consumer prices for liquid milk rose from Rb 30.8 to Rb 32.5 per litre, those for butter – from Rb 239.8 to Rb 285.3 per kg, for hard rennet cheese – from Rb 255.7 to Rb 288.5 per kg<sup>2</sup>.

*Table 38*

**Production of dairy products in 2012-2013 (1,000 tons)**

	2012	2013	Change %
Cheese, cheese products	412.5	389.4	-5.6
Butter	195.3	198.8	+1.8
Whole milk products (in milk equivalent), including	10315.5	10602.1	+2.8
– kefir	780.0	864.1	+10.8
– yoghurt	108.5	114.1	+5.2
– sour cream	525.5	502.0	-4.5
– cottage cheese	366.9	342.0	-6.8
– cream	85.3	93.8	+9.9
Milk in solid forms	117.7	108.6	-7.7
Cream in solid forms	0.3	0.1	-61.1
Dry baby milk (including sour milk) formulas	18.6	17.8	-4.4

Source: Rosstat.

As mentioned above, the reduction of domestic dairy output was compensated by larger import supplies of dried milk and butter.

An essential problem for the Russian market of agricultural and food products is associated with the Customs Union. Transit supplies of “grey” imports come to Russia across the borders of neighboring countries-members of the Customs Union. The major competitor of Russia on the dairy market is Belarus that after the Union's formation has got an unrestricted access to the Russian market. In 2013 Belarus accounted for 77% of the total imports of dried milk and

<sup>1</sup> According to estimates of the National Union of Milk Producers (SouzMoloko).

<sup>2</sup> According to data of FGBU “Spetsstsentruchet v APK” [Federal State Budget Institution “Specialized Center for accounting in the agrifood sector”].

for 41.3% of the total imports of butter<sup>1</sup>. Last year the country also became the second (after Brazil) largest supplier of meat to Russia.

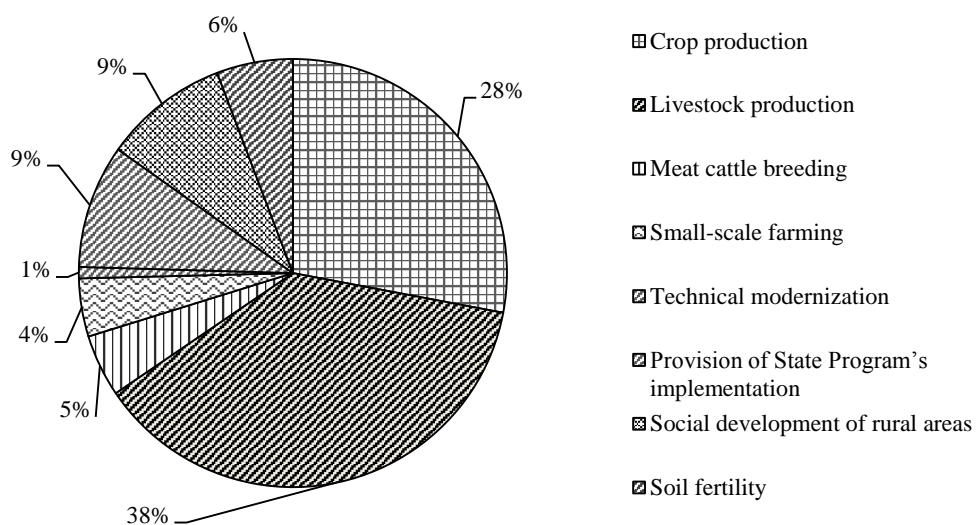
The first year of Russia's membership in WTO showed that natural calamities (drought of the recent years) and the situation on the world markets have a greater impact on the Russian agricultural and food markets than the accession to this organization. Neither essential growth of agrifood imports nor expansion of Russian supplies to foreign markets was observed in 2013. Certainly, some sectors of agriculture being at the stage of active investment development require additional measures to adjust to the new conditions of trade. But it's necessary to understand that the accession to WTO determines prospective trends of the farm sector development: improvement of domestic products' competitiveness versus imported items, market exit by non-efficient producers and further consolidation in the sector, measures for the development of export at the state level (efficiency review, granting of quotas, coordination of veterinary certificates) and re-orientation of state policies towards farm support tools permitted within WTO.

### Implementation of the State Program in 2013

The eight-year State program for agricultural development and regulation of agricultural, input and food markets for 2013-2020 (hereinafter – the State Program) was adopted as a follow-up of the five-year State Program for 2008-2012. It incorporated actually all basic directions and measures of the first State Program. A few directions (such as “Development of meat cattle breeding” and “Support of small-scale farming”) were detached into separate sub-programs while some other measures were merged based on the respective sector (crop production – livestock production). In 2013 the biggest budget infusions were envisaged for the support of livestock production as the priority direction for domestic farm sector development (*Fig. 51*): together with funds for the support of meat cattle breeding it accounted for 43% of the total allocations. It was presumed that following the increase of production and exports of grain, state support would help livestock sector to grow as well. It's noteworthy that the amount of funds envisaged for the State Program's implementation (including expenditures on bureaucratic apparatus) was the same as that for the social development of rural areas (incorporating measures for gasification, water supply, construction of health care and educational institutions all over the country).

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<sup>1</sup> According to data of IKAR for 11 months 2013.



Source: the State Program.

Fig. 51. Structure of financing by basic directions of the State Program in 2013

The global task taken upon by the RF Ministry of Agriculture was the adjustment of the State Program's letter and figure to the commitments assumed by Russia following its accession to WTO. At present 62% of the agricultural budget is allocated to "amber box" measures and 38% - to "green box" measures (Fig. 52).

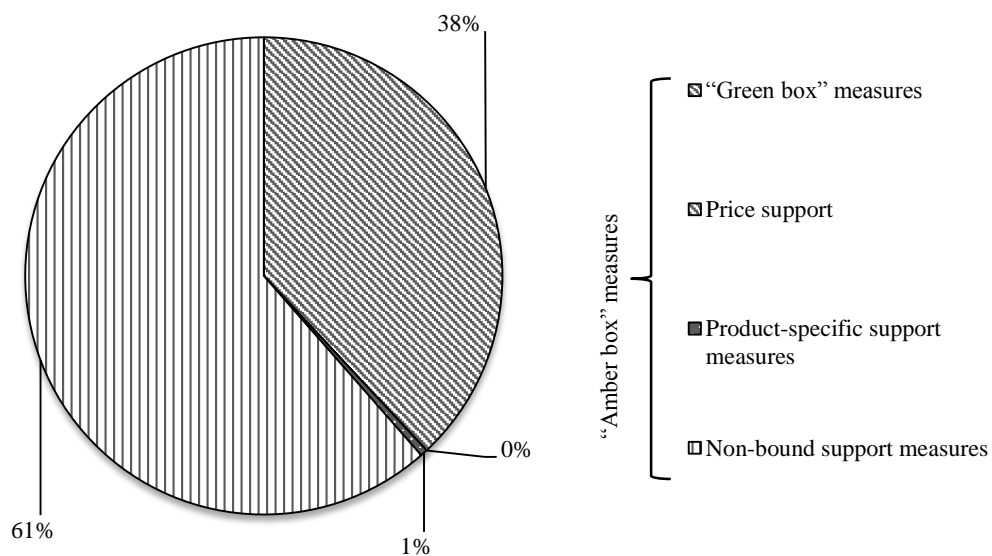


Fig. 52. Structure of farm support in 2013

The reframed support measures are to comply with provisions of Clause 6d Annex 2 of the "Agreement on agriculture", namely: not to be conditioned or determined by types and/or

volumes of agricultural output produced by a specific producer in any year after the base period; not to be influenced by the domestic or world prices for agricultural products produced in any year after the base one. In their turn, investments are to be made only in the agreed period and should not be conditioned by requirements to produce a specific kind of produce (which is pretty often the case in the text of the State Program and associated normative acts. For instance, essential economic programs are financed only in the part corresponding to the announced priority directions such as meat cattle breeding, milk cattle breeding, etc.).

One cannot say that the Ministry of Agriculture has so far failed to make successive attempts to adjust measures of state support so that to exclude them from the most market distorting “amber box”. Some measures for the development of crop and livestock production were shifted into the category of non-bound support including technical modernization of the sector. It is projected to increase the variety and amount of allocations to general support measures, e.g. product marketing and promotion, construction of logistical centers, support to the development of farm cooperation, information and consulting services, systems of market information, other infrastructural projects. As of January 1, 2014 the state support of farm production and social development of rural areas got Rb 197.8bn from the federal budget which is 44% above the respective indicator of the previous year (*Table 39*).

*Table 39*

**Actual amounts of federal budget financing under the first State Program for 2008–2012 by directions, billion rubles**

Directions	2008	2009	2010	2011	2012	2008–2012, % of the projected amounts
Sustainable development of rural areas	8.137	8.963	7.720	7.720	11.000	38.7
Creation of general conditions for farming	17.720	17.737	10.106	11.499	11.800	103.5
Development of priority agricultural sub-sectors	13.144	16.417	10.585	23.129	26.800	116.0
Attaining of financial sustainability of farm sector	78.642	112.270	72.991	74.701	81.000	145.8
Regulation of agricultural, input and food markets	0.639	9.636	5.878	7.934	7.000	Up 4.4 fold
<b>TOTAL</b>	<b>118.3</b>	<b>165.0</b>	<b>107.3</b>	<b>124.9</b>	<b>137.6</b>	<b>118.5</b>
% of GDP	0.28	0.48	0.23	0.22	0.22	

Source: National report on agriculture for 2008-2012. Ministry of Agriculture, 2013; authors’ estimates.

In 2013 the actual financing of the State Program was better than in the previous years (*Table 40*)<sup>1</sup>.

*Table 40*

**Projected and actual financing of the State Program for agricultural development in 2013**

<sup>1</sup> In the 8-year State Program for 2013-2020 the directions of financial support to agriculture were changed as compared with the previous Program and therefore the financing data for 2013 is given separately in *Table 40*. For more details about the shift in directions of state support under the new State Program see Yanbykh R. *Gosudarstvennaya programma razvitiya sel'skogo khozyaystva na 2013-2020: osnovnye napravleniya i problemy adaptatsii k chlenstvu v WTO*. [State Program for agricultural development in 2013-2020: basic directions and problems of adjustment to the WTO membership] // *Ekonomiko-politicheskaya situatsiya v Rossii*. [Economic and political situation in Russia]. 2012, No.7, pp. 49-52.

	<b>Budget item</b>	<b>Envisaged in the State Program, million rubles</b>	<b>Approved budget, million rubles</b>	<b>Actual funding, million rubles</b>	<b>As % of the initial Program projections</b>
1	2	3	4	5	6
1	Partial reimbursement of expenditures on the purchase of elite seeds, on laying out and maintaining of vineyards, perennial fruit and berry plantations, on purchasing and transportation of seeds to the Far North and equated localities, etc.	1960.7	1960.7	1960.6	100
2	Partial reimbursement of interest rate on: - short-term credits (loans) for the development of crop production, processing and marketing	7199.5	19199.5	19175.4	266
	- investment credits (loans) for the development of crop production and processing, development of infrastructure and logistical support of crop produce markets	8785.0	8785.0	13204.7	150
3	Partial reimbursement of farm producers' expenditures on paying insurance fees	5000.0	5000.0	4397.1	87.9
4	Non-bound support to crop producers	15200.0	25200.0	25279.8	166
5	Support of economically viable regional programs in the field of - crop production	3000.0	3000.0	2689.9	89.6

*Cont'd*

	- livestock production	8000.0	8000.0	7255.5	90.7
	- meat cattle breeding	2000.0	2000.0	2000.0	100
6	Support of pedigree livestock breeding	3500.0	3500.0	3558.6	102
7	Subsidies per 1 litre of marketed milk	10000.0	12758.7	12748.1	127
8	Partial reimbursement of interest rate on: - short-term credits (loans) for the development of livestock production, processing and marketing	4094.6	4094.6	4193.4	102
	- investment credits (loans) for the development of livestock production and processing, development of infrastructure and logistical support of livestock produce markets	28740.6	28740.6	34907.2	121
	- investment credits for the building and reconstruction of meat cattle breeding facilities	4424.0	2503.4	0	0
	- long-term, medium-term and short-term credits taken by smallholder farms	5000.0	5000.0	5000.0	100
9	Total amount for the reimbursement of interest rate (2 + 8)	58243.7	68323.1	76480.7	131
10	Renewal of farm machinery inventories	2000.0	7300.0	2430.0	121
11	Forming of state informational resources for ensuring food security	189.7	180.2	128.6	67.7
12	Support to beginner farmers	2000.0	2000.0	2000.0	100
13	Development of family livestock farms	1500.0	1500.0	1500.0	100
14	Partial reimbursement of expenditures of individual private farms (including individual entrepreneurs) on registering ownership titles to agricultural land plots used by them	120.0	120.0	50.7	42.3



15	Federal Target Program “Social development of rural areas till 2013”	9012.3	9012.3	9012.3	100
16	Federal Target Program “Preservation and restoration of soil fertility of farmlands and of agricultural landscapes as the national endowment of Russia in 2006-2010 and for the period till 2013”	7154.3	6625.5	6537.8	91.3
	Total	158942.9	197671.7	197884.6	124

Source: Calculated by authors using data of the Ministry of Agriculture.

The analysis of preliminary results of the first year of State Program’s implementation show that in general measures for supporting livestock production are financed better than those for supporting crop production (*Table 41*). In 2013 the basic subsidies to crop production were for the first time ever granted in the framework of so-called non-bound support per 1 hectare. This measure is less market-distorting and has long been applied in the EU countries. Input support in crop production has been cut to minimum and applies only to specific plantations (vineyards, perennial fruit and berry plantations, purchase of elite seeds, their transportation to the Far North regions, etc.).

The strongest support is rendered in the form of subsidizing credits to farm producers. In 2013 the budget for partial reimbursement of interest rate on all types of credits and loans accounted for 38% of all the allocated funds. This trend could also be tracked in the implementation of the first State Program. Experts have cautioned against a serious problem of accumulating state debts before farm producers on payment of subsidies for the reimbursement of interest rate on investment credits and loans<sup>1</sup>, but the Ministry of Agriculture has so far failed to cope with it. Imbalances in the structure of financing affect other guidelines of the State Program. Year after year such directions as the social infrastructure of rural areas (*Table 39*), smallholder farms and their agricultural cooperation, support of alternative employment in rural areas do not get sufficient funding. In 2013 the most scarcely financed items were the establishment of informational system for ensuring food security and management of agro-industrial complex, the partial reimbursement of expenditures of individual farmers on registering ownership titles to agricultural land plots and the reimbursement of interest rate on credits and loans taken for the development of meat cattle breeding (*Table 40*). There is an impression that due to the extensive commitments for reimbursement of interest rate regional budgets simply get short of funds for other measures. At the same time no funds are allocated from the federal budget unless there is co-financing from the regional budget.

The average share of regional co-financing under all programs is about 26% of the total. However, it differs by directions: for instance under the programs for developing pig production 62.6% of funds were allocated from the regional budgets, under the programs in poultry sector – 36.7%, under the programs of subsidizing investment and short-term credits and loans – 16%, under the Federal Target Program “Social development of rural areas” – 37.7%<sup>2</sup>. In 2013 the total amount of funding from the consolidated budget of the Federation and regions was Rb 267.5bn, or 0.4% of GDP.

<sup>1</sup> Gataulina E.A. *Programma subsidirovaniya protsentnykh stavok: effect i problemy*. [The program of subsidizing interest rates: effect and problems] // *Ekonomika sel'skohozyaystvennykh i pererabatyvayushchikh predpriyatiy*. [Economics of agricultural and processing enterprises]. No.9, 2010, pp. 54-55.

<sup>2</sup> The data on regional co-financing relates to 2012. Source: The National Report on Agricultural Development in 2012.

The budget of Russia's State Program is in general comparable to the US agricultural budget (\$155bn, or 0.93% of GDP). First, the difference in percentage of GDP is not so big (in absolute terms the US budget is 25 fold larger). Second, almost ¾ of the US agricultural budget is spent on programs for improving the structure and quality of nutrition and for ensuring access to it for the most vulnerable groups of population (pensioners, women, children and disabled people). In 2013 allocations to the Nutrition Assistance program amounted to \$111.6bn (72%) while the support to farmers and ranchers – to only \$24.8bn (under the Farm and Commodity Programs)<sup>1</sup>.

Composition of the EU agricultural budget is similar. It amounts to 129.9bn euro or 1.1% of GDP<sup>2</sup> but the biggest part of it goes to various ecological programs including adjustment to the climatic change, food quality and standardization issues, support to producers of bio-safe products, etc.

According to data of OECD, in 2013 the ratio of aggregate support to farm producers to gross agricultural output<sup>3</sup> in Russia was lower than in Europe (13% versus 20%) but higher than in the US (7%).

The tools of state support to agriculture applied in Russia are mostly those regarded as “amber box” measures. When elaborating the new State Program for 2013-2020 the Ministry of Agriculture made attempts to reduce their share. A new support measure was introduced – the support of incomes in crop production. But even after that about 60% of measures remained in the category of “amber box”. If this approach persists, by 2016 the amount of support will come into conflict with commitments taken by Russia when joining WTO. The potential for increasing the level of support is provided in the WTO Agreement on Agriculture<sup>4</sup> but Russia has so far failed to use these mechanisms to their full extent. Attempts to adjust measures envisaged in the effective State Program to the requirements of WTO were made in the study carried out by the Center of Agrarian Policies of the Institute of Applied Economic Research in the Russian Presidential Academy of National Economy and Public Administration<sup>5</sup>. Owing to the alteration of State Program's implementation mechanisms, one has succeeded to transfer support measures to the amount of Rb 83.8bn (\$2.7bn) from the “amber box” to the “green box”, of them 65% are those envisaged for livestock production (Rb 55.3bn). The sub-program for technical and technological modernization has been completely re-channeled to the “green box”. As a result the structure of State Program's budget has radically changed: 24.4% of support still belongs to the “amber box” while 75.6% has been moved to the “green box”. It's obvious that the RF Ministry of Agriculture should carry out a similar job as at present 90.3% of measures applying to livestock production can be labeled as non-market support. The market gets seriously distorted since a specific product is being supported and according to WTO

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<sup>1</sup> The data on US agricultural budget is cited from: Budget Summary and Annual Performance Plan, FY 2013.– USDA.

<sup>2</sup> EUROSTAT: [http://europa.eu/pol/index\\_en.htm](http://europa.eu/pol/index_en.htm)

<sup>3</sup> Producer Support Estimate (PSE): the annual money equivalent of gross transfers from consumers and taxpayers to farm producers estimated at farm gate and attributable to the state support to agriculture irrespective of their nature, goals and impact on the production or incomes of producers. Source: Agricultural Policy Monitoring and Evaluation 2013: OECD countries and emerging economies. – OECD Publishing, 2013.

<sup>4</sup> Agreement on Agriculture. [www.wto.ru/ru/content/documents/docs/selhozru.doc](http://www.wto.ru/ru/content/documents/docs/selhozru.doc)

<sup>5</sup> Shagayda N.I. *Otsenka byudgetnykh raskhodov i byudgetnoy podderzhki v sel'skom khozyaystve Rossii* [Evaluation of budget expenditures and budget support in Russian agriculture] // *APK: ekonomika, upravleniye* [Agro-industrial complex: economy, management]. No. 12, 2012, pp. 14-23.

regulations this is an immediate indication for treating the measure as one from the “amber box”.

So, even in the framework of the existing State program for agricultural development and regulation of agricultural, input and food markets for 2013-2020 there is an opportunity to reduce the amount of most distorting and contradicting WTO rules measures while preserving the basic financial outlays. If all the suggestions for transforming support measures into less market-distorting ones are taken into account, by 2018 the funds for implementing “amber box” support can be cut down to not more than Rb 57,690m (\$1.8bn at the exchange rate effective in early December 2013) which is 2.5 fold below the admissible level declared in the Agreement on Agriculture that Russia signed when joining WTO in 2012.

### Recommendations for policymakers

Recommendations as to the adjustment of agricultural policy following Russia’s accession to WTO are formulated on the basis of analyzing its transformation in the recent decade, the requirements of WTO and the practice of their application in Russia in 2012-2013.

#### ***1. Using principles of WTO and Common Economic Space (CES) for the improvement of domestic agricultural policies***

Having joined WTO and CES, Russia has taken commitments to diminish farm support measures distorting the market and to comply with the set limitations on the amount of such support. The domestic agricultural policies do not envisage similar requirements to regions-subjects of the Russian Federation. Any subject of the Federation has the right to render market-distorting support to home farm producers from the regional budget. The amount of such support is not restricted by either the federal legislation or legislation of the RF constituent members. Moreover, according to the RF Constitution and the effective legislation federal authorities have no competence to introduce such restrictions for subjects of the Federation.

The right of RF regions to support farm producers using “amber box” measures and the active utilization of this right by many subjects leads to the disruption of the national agricultural market. Farm producers from regions with high level of support from the regional budgets enjoy competitive advantages over producers from other regions. As a result the market gets distorted, owing to subsidies the output produced at high cost ousts lower-cost produce from the market.

The priority effort should be the introduction of amendments to Federal Law No.184 of October 6, 1999 “On general principles of organization of legislative (representative) and executive bodies of public authority in subjects of the Russian Federation” that will establish joint responsibility of the Russian Federation and its members for the development of agriculture. It should be envisaged that the federal government is entitled to set mechanisms of control over the level of support to farm producers and to provide for coordination of federal and regional policies of farm support in case international agreements specify restrictions in this field.

#### ***2. Abandoning of compulsory co-financing requirement***

Federal funds for subsidizing any support measure are allocated only on the condition that it is co-financed from the regional budget<sup>1</sup>. In case a subject of the Federation does not have

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<sup>1</sup> *De jure* according to provisions of the above mentioned Law No. 184 FZ measures of the State Program are considered to be financed by subjects of the Russian Federation while the federal budget just co-finances them. But taking into account the federal status of the State Program, the definition of its measures on the federal level

sufficient funds in its budget, regional farm producers lose access to federal funds. This situation infringes the equality of their competitive positions and the integrity of domestic agricultural market, results in the channeling of subsidies to regions with high budget capacities that are often located in areas less fit for farm production. Agricultural producers from regions with lower farm profitability (before subsidies) get more subsidies and credits.

The institute of co-financing extremely complicates the mechanism of State Program's implementation. Financing of any measure under the latter depends on decisions taken by the Federal Assembly, the RF Government, the RF Ministry of Agriculture, authorities of subjects of the Russian Federation, participants of the State Program. The complicated multi-level system of taking decisions on state support requires a long period for coordination. Farm producers usually learn the rates of subsidies for the current year only in autumn.

In order to eradicate these bottle-necks in financing of the State Program, one needs to abandon the institute of compulsory co-financing. Program measures implemented by the federal government bodies should be financed from the federal budget. Regional policies and the availability of funds in the regional budget should not inhibit the receipt of federal subsidies.

This will enable federal and regional authorities to get rid of endless approvals, delays and obstacles to the implementation of planned measures. Besides, all producers in the country will have equal access to federal funds.

### ***3. Guaranteeing of subsidy receipt, discontinuing of restricted and competition-based distribution of subsidies***

According to the Russian legislation a farm producer has the right to apply to the state for subsidies envisaged under the support programs. In case the sum of farm producers' applications exceeds the subsidy limits set for a particular measure in a particular region, the applicant will get a refusal.

Amendments should be made in the law for agricultural development that will guarantee the getting of subsidies. The right to apply for subsidies should be replaced by the right of their guaranteed receipt by all participants complying with the requirements set in laws, the State Program and other regulatory legal acts. In case of subsidy rejection, the farm producer concerned should have the right to turn to the court.

Regulatory acts should clearly specify the state's commitments before farm producers, conditions, rates and guarantees of receiving state support. The terms should be transparent and understandable for farm producers. The access to subsidies should be ensured not by the decisions of bureaucrats but by the law. This will help to cut the number of officials elaborating regulatory acts on law enforcement and taking decisions on the allocation of budget funds as well as to involve more farm producers in measures under the State Program and to lessen corruption in the state support scheme.

The implementation of this approach will require more careful planning of state support measures, the elaboration of mechanisms for rechanneling funds from one measure to another, the forming of a reserve fund that may be needed in case weather conditions are worse than the annual average.

It's obvious that guarantees of granting support to farm producers will work only in case one discontinues the established practice of restricted and competition-based distribution of budget

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and the fact that most funds are allocated from the federal budget, in this paper the allocation of funds from the regional budgets is called co-financing.

funds that results in the infringement of conditions for fair competition and the creation of preferences for some producers.

#### **4. Transfer from product-specific to non-bound support measures**

In Russia a clear preference is given to bound support measures (when the amounts of payments depend on the production volumes or use of inputs, input prices, etc.). In the State Program for 2008-2012 they accounted for 98% of support granted to farm producers. One non-bound support measure appeared in the State Program for 2013-2020 – the subsidizing of incomes in crop production. It accounts for about 10% of the State Program's funds. In the EU non-bound support measures make up two thirds of all subsidies to farm producers.

The transfer to non-bound support measures will liberate such payments from WTO restrictions and help to improve the efficiency of state funds' utilization through:

*a) improvement of the transfer efficiency.* According to economic theory, non-bound measures are more efficient than the support of specific products or subsidizing of inputs. When money is allocated to the rise of product prices or the reduction of input costs, it gets redistributed in favour of product buyers and input sellers. In case farm producers receive subsidies for purchasing fertilizers, the sellers of the latter raise prices and according to studies get about 75% of the subsidy amount while only 25% thereof remains in the disposal of farmers<sup>1</sup>. The situation is similar when the price for a specific product is supported. Processors reduce purchase prices and farm producers lose the granted subventions;

*b) granting more freedom to business in taking decisions.* When the state subsidizes specific products and inputs, it determines the structure of production and input use. Meantime, business is more efficient in performing this mission. For instance, in the process of working out the Priority National Project for 2006-2007 and the State Program for 2008-2012 the decision was taken to subsidize interest rate on credits for agricultural development. The state did not specify for what purposes such credits should be used. Business coped with this task on its own. As a result the major part of subsidized credits was used for the development of poultry and pig production. And these sectors were growing at the rate of 10-15% per annum.

When preparing the State Program for 2013-2020, the government preserved subsidies for the partial reimbursement of interest rate on credits but decided to distribute them by sectors at its own discretion. As a result the bulk of appropriations for subsidized credits is to be channeled to meat and dairy cattle breeding. Since these sectors are loss-making in most farms, business will hardly want to use the provided credit lines for the intended purpose.

#### **5. Incorporation of new “green box” measures in the State Program**

Many “green box” measures envisaged in WTO “Agreement on Agriculture” are not used in Russia at all. Their incorporation in the State Program will help to improve its efficiency. The following “green box” measures are vital for Russia and require state support: *food aid to population, support to income insurance, assistance in case of natural calamities, subsidizing of farms that stop commodity production* (for instance, the program for halting commodity production of poultry meat and pork in household farms for the purpose of controlling avian flu and African swine fever that envisages compensation of respective producers' losses), *subsidizing of input use conservation, subsidizing of structural shifts by encouraging investments, payments under environmental programs, payments under programs of regional assistance.*

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<sup>1</sup> Melyukhina O.G. *Pochemu podderzhka rossiyskogo APK dostatochna, no ne effektivna.* [Why the support of Russian agro-industrial complex is sufficient but non-efficient]. *Agroinvestor*, No.2, 2013.

In the situation of compulsory cutting of pig population in household farms with a view to reduce the risk of disease spread there arises the need, on the one hand, to develop fair mechanisms for compensating the cost of slaughtered animals and, on the other hand, to improve territorial planning in rural areas. In order to support micro-business in rural households it would be rational to work out a recommended practice of spatial planning specifying zones for location of household and individual private farms of different sizes that would enable them to keep livestock and poultry. The specification of such zones should correspond with the size of smallholder farms; the respective regulations should delimitate the number of animals that a farmer can keep on a plot of a certain size so that to comply with sanitary and veterinary norms. It's also necessary to inform rural residents beforehand about the requirements to facilities for keeping livestock and the marginal density of livestock population. Besides, the compulsory limitation of livestock inventories in household farms located in built-up areas is to be accompanied by programs supporting restructuring of small family business in order to alleviate the negative effects for rural families.

#### **6. Rigid restriction of “amber box” measures distorting the market**

“Green box” measures imply soft options of public support when the state creates favourable environment for farm producers by means of general support or encourages certain structural changes.

When applying “amber box” measures the state intentionally plays against market rules, tries to correct market prices, supply and demand. In this case it has to act rigidly, to take on the responsibility for meeting the assumed commitments, to supervise the transfer of state support funds to producers and consumers of farm products rather than to middlemen and other market operators. Let's examine it on the example of grain market regulation.

Article 14 of the Law on agricultural development establishes the mechanism of grain market regulation. It's core is as follows. Each year the RF Ministry of Agriculture is to set minimum and maximum prices for 5 types of grain: milling wheat, feed wheat, feed barley, rye and corn. In case the actual market price falls below the minimum threshold, the state has to protect the interests of grain producers by carrying out purchase interventions, i.e. by buying grain at the minimum price. If the actual market price exceeds the maximum threshold, the state has to protect the interests of grain consumers (in fact the buyers of bread) by carrying out commodity interventions, i.e. by selling grain at the market at maximum price in order to prevent the growth of prices above the maximum level.

So, the declaration of maximum and minimum prices is a strong regulator. Grain consumers and producers make efforts themselves to hold prices from falling below the minimum or rising above the maximum. In case authorities adhere to the taken commitments and nothing extraordinary takes place on the market, the state does not need to buy or sell grain in big quantities. Purchase interventions do not require extensive budget funds.

In fact Article 14 of the Law on agricultural development has turned out to be a “green box” measure since the state does not buy grain from producers at the minimum price (as it was the case in other countries applying this mechanism) but makes a purchase declaration at the exchange. Minimum price is declared as the opening one and then usually follows the Dutch auction. OJSC “United Grain Company” that represents the state in grain purchase interventions at the same time buys grain for its own needs, i.e. for resale. It's obvious that the company is interested in maximum reduction of the purchase prices for grain.

For Article 14 of the Law on agricultural development to really foster “stabilization of prices on agricultural, input and food markets and support of farm producers' incomes” (Paragraph 1

of Article 14) and be an “amber box” measure, one should omit from Paragraph 2 of this article the words “including at exchange auctions”, to specify the date of publishing maximum prices and the terms of pledge transactions.

**7. Increase of support at the account of budget funds and decrease thereof at the account of consumers**

As a result of Russian agricultural policies of the recent decade consumers of farm products have become the main source of aggregate support to agriculture. In 2012 they accounted for 54.1% of this support while only 45.9% were provided by the budget. In the US the share of the budget in aggregate support is as high as 97.6%, in the EU – 82.7%.

In 2010-2012 the aggregate annual support to agriculture in Russia averaged Rb 556.1bn. The funds were provided by consumers of agricultural products – Rb 411.2bn and by the budget – Rb 144.8bn (net receipts). In fact budget expenditures totaled Rb 312.5bn but owing to the support measures Rb 167.7bn returned back (import duties, etc.).

Provided that after the accession to WTO the amount of farm support in Russia remains the same but the structure of its sources comes close to the EU pattern, the appropriations from the budget will need to be increased almost 3.3 fold (from Rb 144.8bn up to Rb 472.7bn).

**8. Support to small business, setting of limits for support to large business**

Measures for the support of agriculture and mechanisms of their implementation are primarily targeted at the support of large business. In spite of declarations about equal rights and equal access to budget subsidies, for small business the latter is actually limited.

In 2010 about 30% of corporate farms and less than 1% of individual farmers and entrepreneurs and consumer cooperatives got subsidies for the partial reimbursement of interest rate on short- and long-term credits of banks and credit cooperatives. The share of smallholder farms in subsidies for mineral fertilizers is somewhat higher: about 3% of individual private farms and entrepreneurs benefitted from them.

The share of small business in the total amount of subsidies is very small: corporate farms and agribusiness companies received about 98% of all subsidies while individual farmers and entrepreneurs and consumer cooperatives accounted for approximately 2% thereof. The only exception were subsidies for fertilizers where the share of smallholder farms reached 12.6%.

The share of 5% of the biggest beneficiaries from budget appropriations was as high as 72.6% of all subsidies on investment credits, 61.6% of subsidies on short-term credits and 47.1% of subsidies on fertilizers.

For the small business to get real state support a whole set of measures need to be taken. The most important of them are listed below:

- a) to specify the categories of farm producers eligible for state support;
- b) to set limits on the minimal size of a farm eligible for state support. Such limits exist in many countries;
- c) to limit the support to large corporate farms and agroholdings. In the EU there is a rule providing that farms with a size of more than 2 thousand hectares are not eligible for support. In the US the upper limit of the total amount of subsidies that can be received from the budget is set at \$300,000.