THE GRAIN SECTOR IN A SITUATION OF NEW EXPORT DUTIES, LOWER PRICES AND HIGH ADMINISTRATIVE BARRIERS

N.Karlova

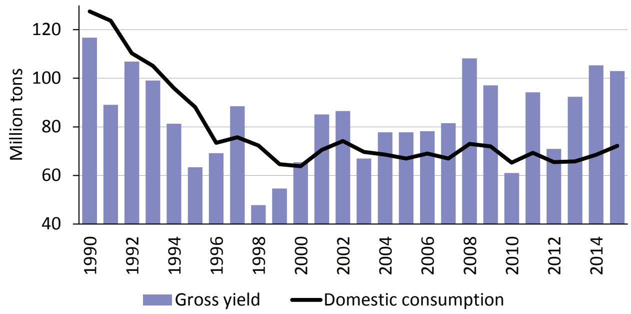
Russia has proved itself a major participant in the global grain trade. On the back of stable domestic consumption and high yields of grain crops in the past few years, grain supplies to international markets have underpinned producers' revenues, engineered technological modernization of the sector and stimulated effective competitive production. In the wake of negative price dynamics on global markets and growth in prices on resources, a variable export duty introduced in 2015 and the existing administrative barriers create the risk of Russia's losing its position as the world's major grain exporter.

Grain is a major agricultural export item. Dependence of the grain sector on the global market is growing. In the past 15 years, the volumes of the grain export have increased 10 times over; it is to be noted that Russia has proved itself as the leading wheat supplier in the Black Sea region. Russia is rated the third in the global trade in wheat after the EU and the US; it is one of the world's five leading producers of wheat. Domestic consumption of grain crop amounts to about 70m tons (*Fig. 1*). In future, it may grow as a result of development of advanced processing of grain into glucose-fructose syrups, however, at present that line is not yet developed as it requires large investments and high-tech production. In a situation of stable domestic consumption and high yields of grain crops in the past few years, grains supplies to foreign markets underpin revenues of producers and create conditions for carrying out technological modernization of the sector and stimulate effective and competitive production.

The regulator of the domestic grain market is the state purchasing interventions which were carried out for the first time in 2001 in order to regulate the general balance of grain on the market. Such interventions are particularly important to producers in Urals and Siberia which do not have access to export markets, while in high yield years of purchasing of grain for the intervention fund support domestic purchasing prices. Southern regions are primarily oriented at export markets. In the 2014–2015 season, the main shipments of Russian grain were carried out through the seaport of Novorossiisk, that is, 32% of the total grain export. It is to be noted that 78% of the total export of grain was shipped through seaports of the Azov and Black Sea basin.

In 2015, the Russian grain market is influenced by the following factors:

- high grain yields in 2014 and 2015;
- depreciation of the ruble exchange rate;
- depreciation of global prices on wheat and other grain crops;



Source: The Rosstat, 2015 – the preliminary estimate of ProZerno.

Fig. 1. Total yield and domestic consumption of grain

- changes in export duties on grain;
- growth in production costs;
- high administrative barriers on the part of the Rosselkhoznadzor and other federal and regional authorities.

According to the data of the Rosstat, in 2014 the yield of grain crops in Russia amounted to 105.3m tons which is the third largest total grain yield in the entire period from 1990s. In 2015, a new high yield of 103.1m tons will be registered this year[1]. In the 2014–2015 season, export supplies in the volume of 31.7 m tons of grain were registered and the above value substantially exceeded average export indices in the 2008–2015 period (*Fig. 2*). In a situation of domestic consumption amounting to about 70m tons, for stimulation of effective and competitive production in the 2014–2015 period at least 30m-34m tons of grain are to be withdrawn from the market for export supplies.

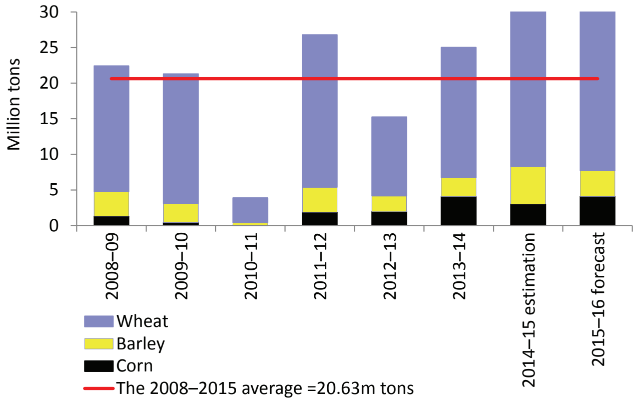
On the one side, a high yield of grain and depreciation of the ruble exchange rate opened up new opportunities to exporters, while, on the other side, trade restrictions in terms of export duties and administrative barriers in a situation of negative price dynamics on global markets and growth in prices on resources

1 The estimate of ProZerno.

contributed to reduction of competitiveness of Russian grain on the global market.

According to the estimates of the Institute for Agricultural Market Studies, as compared to the previous season, growth in production costs per 1 ton of wheat in the 2015/2016 season amounted to 30%. Growth in the cost of production of grain and other sorts of agricultural products is related to changes in the ruble exchange rate. Despite the fact that formally the import component in the pattern of the cost of production of grain is not high, export-oriented suppliers of mineral fertilizers and crop-protection agents form domestic prices on the basis of global market prices. Prices on spare parts for foreign-made machinery appreciated, too. Tariffs on railway carriage increased, while introduction of limitations on the volume of cargo carriage by motor transport (see below) resulted in a 100% appreciation of tariffs on that service. As a result, in the pattern of expenditures the cost of fertilizers and crop-protection agents rose by 46% and 70%, respectively, while the costs on repair and maintenance of capital assets, by 50% (*Fig. 3*).

From February–June 2015, the Russian export of wheat was limited by high export customs duties in the amount of 15% of the customs duty plus 7.5 euros, but minimum 35 euros per ton. From July 1, a new mechanism of export duties on wheat was introduced; in accordance with that mechanism the duty depends on the level of global prices and is determined in the amount of 50% minus Rb 5.500 per ton, but minimum Rb 50 per ton. It was expected that apart from the fiscal nature such a measure will have a regulating effect in the interests of domestic consumers (flour milling plant and other) as regards limitation of the upper level of domestic prices.

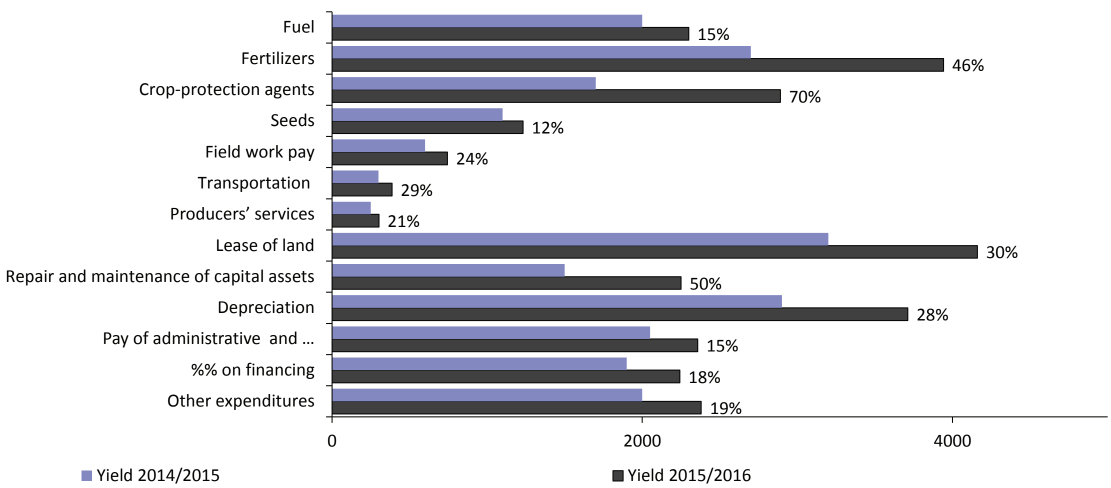


Source: ProZerno.

Fig. 2. The Russian export of main grain crops

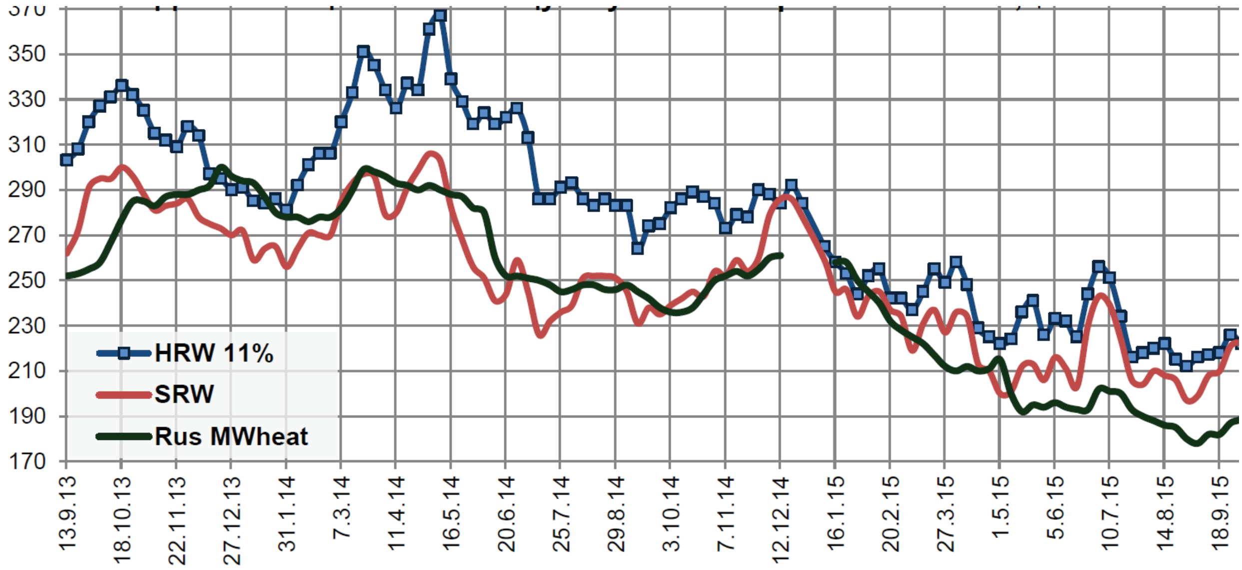
Proceeding from the established procedure for calculation of duties, the exporter pays in any event the minimum amount of the duty of Rb 50 a ton, while in case of an excess of the contract export price of Rb 11,000 a ton the duty withdraws from the export chain nearly 50% of additional ruble revenues. According to market experts[1], direct losses of grain-producing companies from a variable export duty in the 2015/2016 season with preservation of the export volume of the previous season could amount from Rb 1.1bn (with payment of the minimum duty of Rb 50 a ton) to Rb 15.5bn (with the price of $190 a ton and settlement exchange rate of Rb 65 per $1) and that without taking into account additional costs related to the mechanism of application of duties which results in untimely supplies, short supplies and a possible loss of quality of wheat. A key problem of the above mechanism consists in poor foreseeability of the size of the duty on each contract. As export contracts are concluded for several months in advance and changes

1 The estimate of the Institute for Agricultural Market Studies.



Source: The Institute for Agricultural Market Studies.

Fig. 3. Intrafarm costs on production of a ton of wheat in the 2015/2016 season and the 2014/2015 season: The Stavropol Territory and the Rostov Region (export evaluation as of August 2015)



*HRW – winter hard grained and *red grained* wheat, the USA; SRW – winter soft grained and red grained wheat, the USA; RusMWheat – Black Sea food wheat, grade IV.

Source: Prozerno.

Fig. 4. Dynamics of global prices on wheat, USD/a ton (FOB)

in the exchange rate and global prices are difficult to forecast for that period in the current economic conditions, traders have taken a wait-and-see attitude by reducing the extent of purchasing of wheat for export supplies. On the basis of the first months of the new agricultural season (July–September 2015), export supplies of wheat fell in the above months to the lowest indices of export of the past years and were 36% below the volumes of the respective period of 2014.

To support the export potential of Russian grain, from 1 October 2015 the government modified the procedure for calculation of the export customs duty on wheat in accordance with which it amounted to 50% minus Rb 6,500, but minimum Rb 10 a ton. The new level of the duty raises from Rb 11,000 a ton to Rb 13,000 a ton the level of the FOB ruble price on wheat, starting from which the duty is charged and, in its turn, that level is to ensure higher revenues of grain producers. However, the introduced changes do not solve the issue related to activities of customs authorities on spots as the procedure for certification of the contract value of goods is not yet formalized. Overestimated perceptions of customs officials about market prices have an effect not in favor of exporters on the size of export customs duties.

In 2015, a negative factor behind pressure on the grain balance was administrative barriers. High administrative barriers and other regulation-related problems of the agrarian business result in dramatic growth in producers' non-profile costs and reduction of competitive products along the entire chain of supplies. What is meant here is approval of the convention on railway carriage of grain to ports of export; unjustified refusals and delays in issuing of phytosanitary certificates by the Rosselkhoznadzor and system delays in issuing of documents on export shipments of goods which result in risks of additional costs for exporters.

Limitations on load per axle (Federal Law No.248-FZ of 13 July 2015) resulted in dramatic growth in costs related to grain transportation. The law established the responsibility of exporters for exceeding the admissible weight limit or admissible load limit per axle of vehicles in the amount of Rb 500,000. The above limitations result in incomplete load of utilized vehicles which situation leads to growth both in the cost of carriage of a unit of production and additional use of motor transport. It is to be noted that actual costs related to carriage of grain rose by 100%.

From the end of 2014, prices on grain crops have been falling on the global market (*Fig. 4*). Russia is still competitive on the global market as regards price; economic attractiveness of the export is underpinned by depreciation of the ruble exchange rate. However, growth in production costs, introduction of floating export duties and high administrative barriers increase the risk of Russia's losing its share in the global trade in grain.