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Sanctions Likely to Derail the Trajectory of Russia's Agricultural Sector

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Abstract

This article examines the impact of sanctions on Russia's agricultural sector in terms of access to inputs, financing, and export markets. These three factors have been instrumental to Russia's rise as an agrarian power, so their limitation augurs change in Russia's global status.

Strong Performance since 2014

Prior to Russia's unprovoked 2022 invasion of Ukraine, Russia's agricultural sector had been one of the country's few clear economic "winners" since 2014. In six of the eight calendar years starting in 2014, the growth rate for gross product in the agricultural sector exceeded growth in national GDP (based on ruble value). Average annual grain harvests increased from 87 million metric tons in 2008–2013 to 119 million metric tons in 2014–2021. In addition, since 2014 Russia has ranked first or second in the world by volume of wheat exports every agricultural year (Russia's agricultural year runs from July 1 of one year to June 30 of the next year). The dollar value of Russia's agri-food exports rose from \$19.8 billion in 2014 to \$37.7 billion in 2021.¹ Russia's grain trade accounted for nearly 25 percent of global grain trade by volume during the 2020/21 agricultural year.² Analysts within Russia spoke of the nation as an emerging food superpower.

The war with Ukraine and subsequent Western sanctions will interrupt the upward trajectory of Russian agriculture and its export sector. In particular, three key economic factors underpinned the growth of Russia's food production and exports. This article therefore surveys how sanctions will affect access to inputs, financing, and export markets.

Access to Inputs

Agricultural exports depend on the existence of surplus food. Surplus food—the remainder after domestic needs are met—has been generated due to an increase in yields (crops) and productivity (animals). Crop yields have increased due to a rise in the application of mineral fertilizers and the re-mechanization of agriculture.³ The problem for Russia is that it imports a considerable percentage of its agricultural equipment. In 2018, for instance, Russia imported 40% of its agricultural

machinery, although there was considerable regional variation.⁴ In that same year, the annual import market for agricultural equipment in Russia was estimated at \$741 million for tractors, \$505 million for harvesting equipment, and \$427 million for assorted other equipment such as seeders, ploughs, and greenhouse equipment.⁵ The market for agricultural equipment was expected to stay strong until at least 2025 due to government efforts to ensure food security and food self-sufficiency, as well as the need to rebuild the stock of equipment, which had declined precipitously since 2010. To cite just a few examples, the stock of ploughs had declined by 57%, seeders by 52%, tractors by 51%, and grain harvesters by 50% between 2008 and 2018. To rebuild equipment stocks, Russian farms' demand for foreign equipment had been growing, aided by a state program that leased farm equipment at subsidized prices.

Prior to the war, the United States was selling more than \$80 million in agricultural machinery to Russia annually. Following the invasion, the American company John Deere, the largest producer of agricultural machinery in the world, pulled out of the Russian market, which means that previously purchased machinery will not be serviced and spare parts will not be available to Russian farmers. Among European nations, meanwhile, Germany used to lead the way, selling more than \$400 million in agricultural equipment to Russia, followed by the Netherlands, at more than \$225 million annually. The precipitous decline in the value of the ruble against the U.S. dollar and the Euro since the outbreak of war will make the purchase of Western agricultural machinery from third-party sellers prohibitively expensive, likely delaying re-mechanization.

Another input that is vulnerable to the consequences of the Ukrainian war is imported seed. While analysts often cite Russia's impressive increases in crop and grain production over the past 20 years, frequently overlooked

1 <https://www.agroinvestor.ru/analytics/news/37566-eksport-produktsii-apk-v-proshlom-godu-dostig-37-7-mlrd/>

2 Global grain trade was 198.7 million tons of grain in 2021, of which Russia's share was 49.2 million tons.

3 <https://kvedomosti.ru/news/https-mcx-gov-ru-press-service-news-s-nachala-goda-agrarii-narastili-tempy-obnovleniya-parka-selkhoztekhnika-15-6.html>

4 <https://www.trade.gov/country-commercial-guides/russia-agribusiness>

5 <https://yugagro.org/Articles/examining-russias-agricultural-machinery-impo>

is the fact that Russia imports high percentages of the seeds used to grow various crops. Although Russia has devoted significant resources and effort to developing its own seed industry, the country remains dependent on foreign seeds. In 2020, for example, Russia imported 58% of its corn seeds, 73% of its sunflower seeds, and 98% of its sugar beet seeds.⁶ Russia's 2020 Food Security Doctrine states that the country should produce a minimum of 75% of its own seeds. For the 2022 spring sowing, most regions were already supplied with sufficient seed, but if sanctions extend into next year, the following winter and spring planting seasons could be affected.

The dependence on foreign seed is important because the decline in the value of the ruble makes the purchase of imported seeds—just like other inputs—more expensive. Total expenditures on the 2022 planting are estimated at a record high R1 trillion, 20% more than in 2021, owing to rising prices for seed, fuel, and other inputs.⁷ Further, there is no guarantee that Western nations will not cut off access to seeds should sanctions be expanded in the future, although in March 2022 G7 nations indicated that sanctions should not include food trade.⁸

Access to Financing

Grain producers depend on access to subsidies to fund purchases of fuel, fertilizer, seeds, and pesticides during their sowing seasons. For several years, the primary form of state support for agriculture has been subsidized credits and loans. The spring 2022 sowing season witnessed two main problems. First, because of the increase in the price of seeds, fertilizer, fuel, and other inputs, a change in the subsidy process was enacted by the Ministry of Agriculture whereby subsidies were to be allocated prior to planting rather than afterwards, as had been the custom. However, as of mid-March 2022 only five regions had changed their legislation to allow subsidies to be allocated as a monetary advance. As a result, less than 3% of the R127 billion allocated by the federal government to support spring sowing had actually been distributed by regional governments, a fact that was greatly impacting the progress of the spring sowing in certain areas.⁹

The difficulty in obtaining subsidy advances affected agroholdings, which are the largest, most modernized,

and most productive farms in Russia. They are located mostly in the south, which generates the most agricultural production. Agroholdings reported difficulties obtaining foreign pesticides for their crops due to rising prices (a reality that dated back to fall 2021) and a lack of deliveries from foreign suppliers in March 2022.¹⁰ The shortage of pesticides is important because their application has a direct impact on yields and total output. This is especially true in southern Russia, where air temperatures are higher and are rising due to climate change, since warmer temperatures increase the presence of insects, locusts, and other pests.

The second problem with financing is that after Russia's Central Bank raised its interest rate to 20% in late February, all loans became more expensive. Although interest rates on agricultural loans are subsidized, the increase in the Central Bank rate means that the cost of borrowing rose as much as 17%.¹¹ The increase in the cost of borrowing, combined with more expensive inputs across the board, puts financial pressure on farms.

Access to Markets

With food security for several basic commodities ensured, starting in 2018 the Russian government emphasized an increase in food exports. Various efforts toward that goal paid off as the dollar value of food exports reached a record almost \$38 billion in 2021; in that same year, Russia sold food to 160 countries worldwide.¹² In addition, in 2021 Russia continued to expand the number of its agricultural attaché offices in different countries from 23 to 31.¹³

Restrictions on export trade can be traced to early 2020, when global food prices began to rise, prompting Russia to renew its emphasis on domestic food security. In April 2020 Russia placed an export quota on various grains that ran to the end of the agricultural year (June 30). In 2021, Russia again imposed an export quota on grains for the second half of the agricultural year and also introduced a floating export tariff on wheat in June 2021 that has remained in effect since then. The export tariff is equal to 70% of the difference between \$200 per ton and the contract price. The floating tariff means that it adjusts in line with changes in contract prices, which are influenced by world market prices. As global wheat prices rose in the second half of 2021, Russia's

6 <https://agrovesti.net/news/indst/v-rossii-predlagayut-ogranichit-import-semyan.html>

7 <https://www.agroinvestor.ru/analytics/news/37721-zatraty-na-posevnyu-v-etom-godu-dostignut-rekorda/>

8 <https://dairynews.today/news/strany-g7-sanktsii-protiv-rf-ne-dolzhen-prepyatstv.html>

9 <https://www.agroinvestor.ru/analytics/news/37704-agrarii-stolknulis-so-slozhnostyami-pri-poluchenii-avansovykh-subsidiy/>

10 <https://www.agroinvestor.ru/markets/news/37670-agrokholdingi-soobshchili-o-slozhnostyakh-s-zakupkami-sredstv-zashchity-rasteniy/>

11 <https://agrovesti.net/news/indst/agrokholdingi-stolknulis-s-problemami-po-zajmam-s-playayushchej-stavkoj.html>

12 <https://agrovesti.net/news/indst/rossiya-v-etom-godu-eksportirovala-produktsiyu-apk-v-bolee-chem-160-stran-mira.html>

13 <https://mcx.gov.ru/press-service/news/minselkhoz-rossii-rasshiryaet-set-attashe-po-apk-za-rubezhom/>

export tariff also increased, eventually costing exporters R92 billion.¹⁴ The export tariff put downward pressure on exports: during the first half of the 2021–22 agricultural year—the part of the season when exports are highest—the volume of grain exports fell by more than 24% compared to the same period in the 2020/21 season.¹⁵

On February 15, 2022, a previously planned export quota went into effect that limited sales to states outside the Eurasian Economic Union (EAEU) to 11 million tons of Russian grain (including 8 million tons of wheat). The quota will run until June 30, 2022. But after the war broke out, the Russian government on March 10, 2022, introduced a temporary ban on the export of grains—wheat, rye, barley, and corn—to countries in the Eurasian Economic Union. This will remain in effect until June 30, 2022.¹⁶ Contracts signed before the ban were allowed to be fulfilled.¹⁷ This restriction was adopted “to protect the domestic food market” and to prevent the resale of Russian grain by EAEU nations to third-party nations.¹⁸ An additional ban on the export of white and raw sugar to countries outside the EAEU will be in effect until August 31, 2022.¹⁹ Although nations in the EAEU are not among the largest purchasers of Russian wheat, the ban on wheat exports will affect Russia’s overall export levels.

Beyond administrative restrictions on grain exports, sanctions are an important restraint on Russia’s grain trade because Western purchasers do not want to do business with Russian grain companies. Accordingly, the forecast for Russia’s grain exports during the 2021/22 agricultural year (July 1, 2021 – June 30, 2022) was lowered to 28 million tons of grain and 23 million tons of wheat, a more than 30% decrease from 2021.²⁰ For comparison, during the 2020/21 agricultural year, Russia exported 49 million tons of grain, including more than 38 million tons of wheat.

About the Author

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The countries with the most to lose from any reduction in Russian grain exports are those in the Middle East and North Africa (MENA). Egypt is the world’s largest importer of wheat, more than 80% of which it buys from Russia and Ukraine. Turkey also buys large amounts of Russian cereals. These and other authoritarian countries throughout the region depend on Russian grain not only to maintain food supplies, but also to subsidize bread and other grain products. As global grain prices rise, it puts financial pressure on those governments to maintain subsidy levels. The last time the region experienced the combination of a spike in global grain prices and tight supplies, the popular uprisings known as the Arab Spring occurred, bringing about regime change in Tunisia, Egypt, and Libya, and setting off a civil war in Syria that continues to this day. The curtailment of Russian wheat trade will also affect Afghanistan, Yemen, and Ethiopia, which are experiencing high degrees of food insecurity and even localized famine.

Conclusion

Since 2014, Russia has become a central player in the international food market, ranking first or second in wheat exports every year. Russia’s war with Ukraine and Western sanctions jeopardize the government’s goals for the agricultural sector, as expressed in the current State Program for 2019–2025. Specifically, the goal of raising grain output to 140 million tons annually by 2025 will confront difficulties when it comes to importing high-yield seed, spare parts for machinery, and pesticides. Western sanctions on the Russian economy and the freezing of its overseas assets will also make previous levels of subsidization of agriculture difficult. The goal of increasing food exports to 150% of the 2020 level by 2024 will surely not be attained, as domestic food security takes priority.

14 <https://agrovesti.net/news/indst/byudzhet-rf-poluchil-v-2021-godu-pochti-92-mlrd-rub-ot-eksportnykh-poshlin-na-zerno.html>

15 <https://agrovesti.net/news/indst/eksport-zerna-iz-rossii-s-nachala-2021-2022-selkhozgoda-snizilsya-na-24-4.html>

16 <https://dairynews.today/news/pravitelstvo-vvelo-vremennyy-zapret-na-eksport-sakh.html>

17 <https://agrovesti.net/news/indst/minselkhoz-uprostit-eksport-semyan-po-kontraktam-zaklyuchennym-do-zapreta.html>

18 <https://agrovesti.net/news/indst/kak-zapret-eksporta-zerna-iz-rossii-mozhet-stat-chastyu-vojnny-sanktsij.html>

19 <https://agrovesti.net/news/indst/kabmin-vvel-vremennyy-zapret-na-eksport-zernovykh-v-strany-eaes-i-sakhara-v-treti-strany.html>

20 <https://agrovesti.net/news/indst/rossiya-k-10-marta-snizila-eksport-pshenitsy-na-30-9-do-23-mln-tonn.html>

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