EXECUTIVE BRIEF: Market Impacts of Russian Export Ban

August 20, 2010

- A Russian export ban and news that world wheat production would be down five percent in 2010-11 led to a sharp upward adjustment in wheat prices in international markets between July and August.

- But, considering the sizeable wheat stocks held in major exporting countries after two bumper harvests, particularly in the United States, and a likely supply response by cereal producers, prices will likely ease over the medium term.

- However, in Central Asia, wheat importing countries—Afghanistan and Tajikistan in particular—are likely to be negatively affected by reduced regional supplies, export restrictions in exporting countries, and higher prices.

Summary of the Wheat Supply Shock

Acute dryness and heat in Russia and Kazakhstan, heavy rainfall in Ukraine, and abnormally dry and hot conditions in Europe have caused a sizeable reduction in potential 2010-11 wheat production. According to the United State Department of Agriculture (USDA), wheat production in Russia, Kazakhstan, and Ukraine will decrease by 16.7, 5.5, and 3.9 million metric tons (MMT), respectively, compared to last year. Yields will also be lower in Canada, due to excessive rainfall, (6 MMT lower than last year) and other parts of the world. As a result, world wheat production is expected to drop by 34.6 MMT compared to 2009-10, a 5 percent decline, despite prospects for good production in Argentina, Australia, China, India, Turkey, and the United States.

In addition to declines in production, Russia has enacted an export ban on wheat grain, flour, and coarse grains as of August 15. Although the government of Kazakhstan, a major supplier of wheat flour in Central Asia, had maintained its wheat export plans in Central Asia as of mid-August, it might eventually align its trade policy with that of Russia by banning grain and flour exports. Ukraine could also decide to implement a quota on exports of 2.5 MMT in late August, a figure significantly below the quantity it exported in 2009.

Impact on International Markets

In July, a downward revision of wheat production prospects in the Black Sea region led to soaring wheat prices in international markets. The price of U.S. No. 2 Hard Red Winter Wheat (fob, U.S. Gulf) rose 44 percent between the week ending July 2 and the week ending August 6, from USD176 to USD254. The price of Soft Red Winter Wheat increased in a similar fashion. These price increases are comparable to those that occurred during the periods May – June 2009, when the reference price above reached USD294, and October – November 2009. However, they remain smaller than the increases observed during the food price crisis of 2007 – 08, when the price of hard winter wheat peaked at USD510.

Between late July and early August, wheat futures prices for the September and December 2010 contracts traded at the Chicago Board of Trade also showed significant increases, comparable to the movements seen during the food price crisis. But the prices of contracts maturing farther into the future increased more slowly, indicating that market participants expected a moderation in prices in the medium term. Furthermore, futures prices declined in the middle of August. Hence, while markets adjusted to the news of lower prospects for world wheat supplies, recent price trends suggest that market participants do not anticipate a major imbalance between supply and demand.

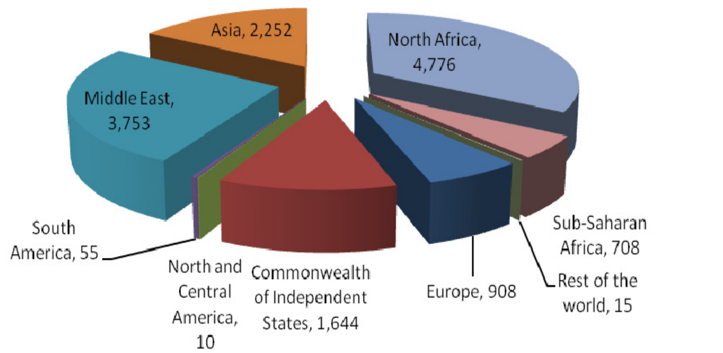
World wheat stocks have substantially increased for the past two years. Global stocks at the end of the marketing year 2009-10 are estimated at 194 MMT, 70 MMT greater than in 2007-08 and much larger than the projected production shortfall. The stocks held in the U.S. are particularly large, while within the former Soviet Union region, stocks are almost twice as large as in 2007-08. The five-percent decline in world production must also be considered in the context of two consecutive bumper harvests, in 2008-09 and 2009-10. Furthermore, a supply response is expected for spring wheat in the southern hemisphere, in South America (Argentina in particular) and Australia, and for winter wheat in the northern hemisphere, which would likely bring wheat prices down if they were to remain high (although the prices of other grains and pulses would increase because of reduced planted area).

Expectations of decline in the production of other cereals due to adverse agro-climatic conditions have also led to an increase in the price of coarse grains (barley, maize, and rye), Russia being a major producer and exporter of barley. For rice, expectations of above-normal rice harvests in the major exporting countries (Thailand, Vietnam, and the United States) and other countries (Indonesia, the Philippines, and Bangladesh) and the anticipated marketing of large stocks in Thailand and India are maintaining prices at relatively low levels.

Impacts in Africa and South/Central Asia

Over the past decade, Russia has become a major player in wheat export markets. With wheat production figures just below U.S. production levels, Russia exported 27 percent of its annual output over the past five marketing years, on average. In 2009-10, Russia shipped 17.5 to 18.7 MMT of wheat to export markets, according to different sources, which accounted for about 10 percent of world exports. The Middle East and North Africa regions represent the largest importers of Russian wheat (see Figure 1). Over the past five marketing years, of total annual exports to the Middle East, 17 percent went to Yemen and annual exports from Russia to Yemen amounted to 456,000 MT on average. This year, the Middle East and North Africa will substitute imports from other large exporters, in particular the U.S. and the EU, for imports from Russia, but at a higher cost. Countries such as Yemen are thus vulnerable to significant wheat price increases.

Figure 1. Destination of Russian wheat exports (five-year average, in 1000 MT)



Source: *International Grains Council*

Asia is also a major market for Russian wheat, in particular Central and South Asia. Over the past five marketing years, an important share of exports from Russia to Asia went to Pakistan. This country could suffer from the combined effect of crop losses due the floods and the high cost of imported wheat following the contraction in wheat export supply from Russia and Kazakhstan. Exports to Afghanistan accounted for just three percent of annual exports to Asia, the five-year average for wheat exports to Afghanistan amounting to 68,000 MT. The reliance of Afghanistan on Russian wheat is thus limited, but in combination with the decrease in exports of wheat flour from Kazakhstan, local markets might experience significant increases in wheat grain and flour prices. Tajikistan faces a similar situation. For Afghanistan, Tajikistan, and Pakistan, greater imports from Uzbekistan, where production is expected to be normal, could mitigate the price impact of the decrease in imports from Russia and Kazakhstan.

In Afghanistan, wheat prices have slightly increased throughout the country between June and July. In Mazar, in the north (where most of the imported wheat comes from Uzbekistan and Kazakhstan), the price of wheat grain rose eight percent between June and July. In Pakistan, price increases of 15 to 20 percent have been reported, although this may be in large part due to the floods. In Khujand, in northern Tajikistan, near an important entry point for wheat grain and flour imported from Kazakhstan through Uzbekistan, the prices of wheat grain, imported flour, and local wheat flour increased by about 10, 25, 35 percent, respectively, between July 7 and August 4 (WFP). These price movements are moderate in comparison to the price hikes observed in 2009 and 2007-08. Given the good production prospects in Tajikistan and Afghanistan and the fact that prices have been relatively low in 2009-10, the impact on food security in the short term is likely to be minor. However, a disruption in southward trade flows in Central Asia during the marketing season might result in more pronounced price increases in the medium term, with potentially significant food security implications in 2011, in the months preceding the harvest. Thus, trade measures and their impacts should be monitored carefully. In Tajikistan, exports of grain to Afghanistan and Uzbekistan channeled through the Kathlon region in the south have been banned until 2011 after Russia announced a ban on grain exports.