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Economic Cooperation in Agricultural Sector of CIS Countries



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The Author:

Murat Jadraliyev

Senior Analyst, Economic Analysis Unit, EDB
E-mail: Jadraliyev_ma@eabr.org
Telephone: +7 (727) 244 40 44, ext. 6902

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Coordinator:

Gulnaz Imamniyazova, EDB

Address:

Eurasian Development Bank

Dostyk Ave. 220, Almaty, 050051,
Republic of Kazakhstan
Telephone: +7 (727) 244 40 44
Fax: +7 (727) 244 65 70, 291 42 63
E-mail: editor@eabr.org
<http://www.eabr.org>

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Abbreviations

ASEAN – Association of South East Asian Nations
CA-4 – Kazakhstan, Kyrgyzstan, Uzbekistan and Tajikistan
CIS – Commonwealth of Independent States
ETS – Eurasian Trading System
EurAsEC – Eurasian Economic Community
EurAsEC-3 – Belarus, Kazakhstan and Russia
EurAsEC-5 – Belarus, Kazakhstan, Kyrgyzstan, Russia and Tajikistan
FAO – UN Food and Agriculture Organisation
FDI – foreign direct investment
GDP – gross domestic product
IPO – initial public offering
ITC – international transport corridor
JV – joint venture
MERCOSUR – Common Market of the South
NAFTA – North American Free Trade Area
OPEC – Organisation of Petroleum Exporting Countries
RCS – Russian Commodity System
RFCA – Regional Financial Centre of Almaty
RMA – Russian Ministry of Agriculture
SES – Single Economic Space
SES-4 – Belarus, Kazakhstan, Russia and Ukraine
SIEI – EDB's System of Indicators of Eurasian Integration
SPO – secondary public offering
TNC – transnational corporation
UNCTAD – United Nations Conference on Trade and Development
WTO – World Trade Organisation

Main Conclusions

1. **Sectoral economic cooperation and integration are powerful tools that can enhance the competitiveness of farm produce.** Mutual investment would support production, whereas integration initiatives (establishing the Grain pool and the Customs Union and joining the WTO in a coordinated manner) would help the agricultural sector to meet the challenges it faces.
2. **Mutual investment in agribusiness is insignificant; the main source of investment is Russia.** Foreign investment in agribusiness may efficiently replace public investment, but to date they make up a negligible percentage of the total investment in this sector. This can be explained, first of all, by the fact that agribusiness is not nearly as attractive to potential investors as other sectors, and secondly by the absence of a system stimulating FDI in agribusiness. Mutual investment in agribusiness by the countries under review are also insignificant; the main source of investment is Russia, whose main investment targets are Belarus, Ukraine and, to a lesser extent, Kazakhstan. Kazakh investors are also active in this sector. The major investors are large Kazakh and Russian cereals producers.
3. **Agricultural and transport infrastructure, grain, meat and milk processing and farm machinery are all priority targets for mutual investment.** In our opinion, the priority targets for investment are export infrastructure (i.e. developing optimal routes to target markets, raising the capacity of grain terminals, etc.), large international grain, meat and milk production assets (the notion of an “Eurasian Agricultural Transnational Company” and the manufacture of farm machinery in the countries under review).
4. **The countries under review are net grain exporters and net meat importers.** During 2000–2008s the aggregate share of Kazakhstan, Russia and Ukraine in global grain production increased from 6% to 24%. Most of their grain output is being exported to remote markets: South Asia, the Persian Gulf, North Africa and the EU. Belarus, despite its extensive domestic production, imports 400,000–500,000 tonnes of cereals from other countries. All countries under review are highly dependent on meat import from remote markets (the Americas).
5. **Kazakhstan is a leader in cereals trade integration.** An analysis of export and import of cereals in the EDB’s System of Indicators of Eurasian Integration (SIEI) suggests that Kazakhstan takes the lead among four countries under review. Mutual trade of cereals by these countries is declining over time, whilst export to remote markets is increasing.
6. **All the stakeholders need the Grain pool and will benefit from it.**

The sound potential of the countries under review is weakened by competition with other grain exporting countries and, primarily, between themselves. This competition reduces the efficiency of their actions and deteriorates the outlook for better positions in the global markets. As a result of their mutual competition, Russia, Kazakhstan and Ukraine lose \$10–20 on each tonne of grain. Realising their export potential and strengthening their positions in global grain markets will require concerted efforts, a common export policy, and a developed infrastructure. The initiative by Kazakhstan, Russia and Ukraine to establish the Grain pool will be an efficient vehicle to achieve this goal. **Creating the Grain pool is a cumbersome process; this is likely to be a long drawn-out process.** Kiev’s unclear stance on the Grain pool, shifting under political pressure from the EU, may undermine this initiative. Under a pessimistic scenario Kiev will refuse to participate, and without Ukraine the economic benefits for Kazakhstan and Russia will be insignificant. Another scenario could be that the establishment of the Grain pool may take several years.
7. **“In a coordinated manner, but not together”: the optimal position for the Customs Union in negotiations over joining the WTO.**

If the countries under review join the WTO making the maximum concessions possible, this will mean unrestricted access for imported products to their domestic markets whilst the developed countries’ markets will remain closed. This in turn will undermine their efforts to develop competitive farm production. On the other hand, joining the WTO in coordination with a major political and economic player such as Russia will enable Kazakhstan and Belarus to secure themselves more beneficial terms of accession.

1. Introduction

The role of agribusiness in the region's economy could not be overstated. Agribusiness and, essentially, farm production make up a big share in CIS countries' GDP. Although this share is tending to decline due to the expansion of other industries and presently does not exceed 7–8% in some of these economies (see Table 1.1), agribusiness retains its vital role.

Share in GDP (%)	2000	2001	2002	2003	2004	2005	2006	2007	2008
Russia	7.1	6.9	6.7	6.8	6.0	5.2	4.9	4.9	4.5
Kazakhstan	8.1	8.7	8.0	7.9	7.1	6.4	5.5	5.7	5.6
Belarus	11.6	10.1	9.6	9.0	8.4	7.5	7.5	7.4	8.3
Ukraine	9.6	9.1	8.9	8.6	10.8	9.2	8.4	7.4	8.6

Table 1.1.
The share of agribusiness in GDP in some CIS countries

Source:
the national statistics agencies of Belarus, Kazakhstan, Russia and Ukraine

The agricultural sector is responsible for national food security, and self-sufficiency in the domestic supply of farm production (or, at least, its basic items) is a sign of a healthy economy. Just as importantly, agricultural sector is the main source of employment in many CIS countries: despite the global trend towards urbanisation (which is also pronounced in the post-Soviet world), the majority of the population still lives in rural areas.

Finally, agriculture and agribusiness have a multiplier effect on an economy. For example, according to the input-output balance of Russia, one rouble worth of farm produce generates 1.16 roubles in related industries: mechanical engineering, chemistry, extractive industries, transport and communications. Moreover, one million roubles worth of farm produce allows 23 new jobs to be created in related industries¹. It can be safely said that, due to this multiplier effect, any measures to support agribusiness have a tangible anti-crisis effect.

The definition of agribusiness is complex, and it is not really possible to discuss all issues relating to cooperation in this sector within the CIS in a single paper. Therefore, we have reduced the number of countries under review to four: Belarus, Kazakhstan, Russia and Ukraine. The rationale for our selection is as follows:

- these four countries are the key players in agribusiness in the post-Soviet world, and account for over 85% of the area of the former Soviet Union;
- these countries are the CIS² leaders in terms of arable and farm land;
- the agricultural sector in these countries has largely the same structure (compared to other CIS countries), and these countries are major suppliers of farm produce.

Apart from this geographic limitation, we will further confine our discussion to cereals, meat and milk production, i.e. the segments which have strong potential for the development of mutual trade, investment and corporate integration.

¹ At the exchange rate as of 01.12.2009. The EDB's calculations are based on the input-output balance of Russia.

² Actually, the area of Turkmenistan or Uzbekistan (447,000 and 407,000 km respectively) is nearly double the area of Belarus. However, we excluded these countries from our review, because their statistics are largely incomplete or questionable. In addition, Belarus is a member of the EDB and takes an active part in all major post-Soviet integration initiatives.

Integration issues related to agriculture development will be discussed in three sections:

- 1) The investment policy is the key to sustainable development of agriculture in the countries under review; investment in our context includes government support to the sector (as part of national investment projects) and foreign direct and mutual investment. In this review we will elaborate on mutual investment as an important component of integration.
- 2) Expanding mutual trade at the regional level and developing efficient production chains and intraregional division of labour can help enhance the competitiveness and export potential of domestic farm produce in global markets; in the respective section we will assess the current status of and prospects for mutual trade in the region's agricultural sector.
- 3) The institutional component includes various joint initiatives by the countries in the region. Particularly, we will focus on the initiative by Kazakhstan, Russia and Ukraine to establish the Grain pool.



2. Mutual Investment in Agribusiness

2.1. Foreign Investment in Agribusiness

The current governmental agriculture development programmes envisage significant investment, yet in themselves they are not sufficient for the creation of a competitive and efficient agricultural sector. Foreign investment, in our opinion, should become an additional mechanism for the development of agribusiness, processing facilities and related infrastructure, and transferring technology.

Due to a number of factors, both domestic and foreign companies began to pay closer attention to the agricultural sector in developing countries in recent years.

The main factors that stimulate investment in agriculture are the availability of land and water in certain regions and the rapid increase in demand and import of crops to some countries, including Brazil, India, China, Russia, and South Korea. The international demand for investment in agriculture also increased as a result of new initiatives relating to eco-fuel, which resulted in an influx of capital into the production of cereals, sugar cane and oil-bearing crops. This trend was coupled with a rapid increase of food prices following an increase in consumption.

Globally, foreign investment in agriculture is on the rise, although the total amount remains relatively low — some \$32 billion in 2007 (UNCTAD, 2009). Whereas in the early 2000s foreign investment was principally in the production of food and drinks, at present transnational companies also invest in farm production, thus expanding their presence in this sector even further.

Region	FDI flows				Total			
	Inflow		Outflow		Imported capital		Exported capital	
	1989–1991	2005–2007	1989–1991	2005–2007	1990	2007	1990	2007
Agriculture, forestry and fishery								
All countries	0.6	3.3	0.5	1.1	8.0	32.0	3.7	10.2
Developed countries	–0.01	0.04	0.5	0.6	3.5	11.8	3.4	7.5
Developing countries	0.6	3.0	0.05	0.5	4.6	18.0	0.3	2.4
Southeast Europe and the CIS		0.3		0.05		2.2		0.3
Production of foods and drinks								
All countries	7.2	40.5	12.5	48.3	80.3	450.0	73.4	461.9
Developed countries	4.8	34.1	12.2	45.7	69.9	390.7	73.1	458.1
Developing countries	2.4	5.1	0.3	2.6	10.4	46.9	0.3	3.5
Southeast Europe and the CIS		1.4		–0.01		12.4		0.3

Table 2.1.
Assessments of FDI in agriculture, forestry, fishery and the food industry (\$ billion)

Source:
UNCTAD (2009)

The amount of foreign direct investments (FDI) in agriculture as part of the total FDI structure remains insignificant in most countries with the exception of some of the least developed ones (Cambodia, Laos, Malawi, etc.). At the same time in Indonesia, Malaysia and Ecuador the significant share of FDIs in agriculture is attributable to both external factors and the national policy aimed at encouraging investment in this sector. According to UNCTAD, Ukraine (4%) and

Russia (1%) occupied the 10th and 21st positions, respectively, among the forty states which had the highest shares of FDI in agriculture in 2005–2007s (UNCTAD, 2009). Belarus and Kazakhstan were not listed.

In developed countries, most FDI in agriculture is intended for the production of food and export crops; interest in eco-fuel crops is also increasing. There is also a trend towards regional specialisation among recipient countries depending on their staple products. For example, in “transition economies” which include Belarus, Kazakhstan, Russia and Ukraine, foreign investors focus on milk products, although in recent years investments in wheat and other cereals were on the rise.

In *Russia*, the main sources of FDI in agribusiness are Cargill, Nestlé, Bunge, Coca-Cola, Kraft, Mars, PepsiCo, Tetra Pak, British American Tobacco and Unilever. In 2005–2008s total direct investment by these companies in projects launched or completed in Russia exceeded \$1.8 billion. These investments were used to build new modern facilities or modernise and expand existing ones. Such newly built or modernised assets meet all environmental and quality standards (RMA, 2009).

In *Kazakhstan*, the percentage of FDI in agriculture has tended to decline in recent years, whereas the share of farms’ investments in their own fixed assets increased. The level of FDI dropped from 13.4% in 2003 to mere 0.1% in 2007, and then increased to 0.6% in 2008 (see Table 2.2, Figure 2.1); despite the percentages involved this information remains within the range of statistical accuracy.

Table 2.2.

Sources of investments in privately and publicly owned fixed assets in agriculture in Kazakhstan (in actual prices, million tenge)

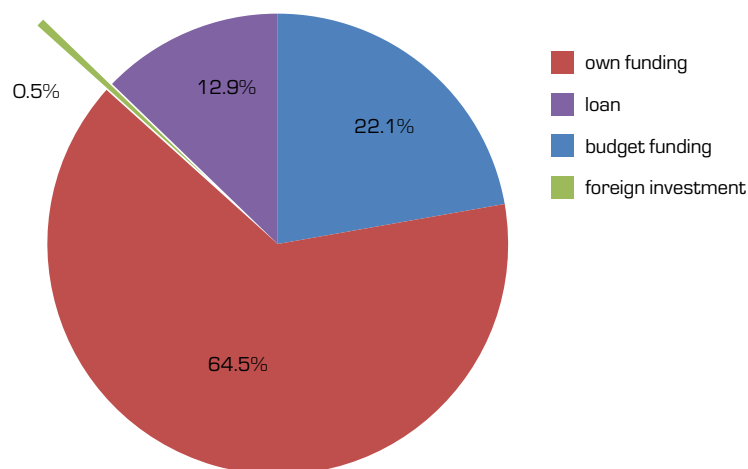
Source:
The Statistics Agency of Kazakhstan

Year	Investments in fixed assets	Sources				
		National budget	Local budget	Foreign	Other borrowings	Farms’ own capital
2003	25513	3192	197	3421	1778	16925
2004	43844	3789	347	4973	3012	31724
2005	47976	5396	1417	4378	6188	30598
2006	47144	11127	1453	1865	4446	28252
2007	55973	11078	3388	72	9928	31507
2008	77772	13231	4258	498	10754	49031

There were some isolated cases of investment activity in the meat and milk sector in Kazakhstan. For example, in 2009 Lactalis of France purchased the assets of FoodMaster International in Kazakhstan, Moldova and Ukraine. According to available information, 80% of the shares in FoodMaster were sold by Agribusiness Partners International, a US investment fund which had been one of the founders of this holding company.

However, during the first four months of 2009 foreign investments in Kazakhstan’s agricultural sector totalled mere 3 million tenge (about \$20,000) (see Figure 2.1) — a huge retrograde step after an increase by 24% in the same period in 2008. In crisis conditions, the fact that agriculture holds little appeal as a potential target for investment and cannot offer a quick payback aggravates its situation, and this warrants efforts to secure alternative sources of capital.

In 2006–2008s *Ukraine* saw a dramatic increase in foreign investment in agribusiness. Thus, from June 2007 to June 2008 Ukrainian agribusiness companies received in investment nearly half of the total amount generated by all share placements by the companies from all sectors of the economy (\$1.14 billion). From the end of 2006 to the present, Ukrainian agribusiness companies completed four IPOs, two SPOs and six private placements, generating

**Figure 2.1.**

The structure of investments in Kazakhstan agribusiness in 2008 (%)

Source:

The Statistics Agency of Kazakhstan (2009)

a total of \$1.18 billion (Golubeva, 2008). These companies secured themselves favourable assessments from investors despite the global liquidity crisis — largely due to the generally high level of development of the national agricultural sector.

2.2. The Monitoring of Mutual Investment

An analysis of foreign investment in agriculture in recent years shows that these flows are not significant. What countries can be viewed as prospective sources of foreign investment? In our opinion, the emphasis should be made on mutual investment by the countries under review. Mutual investment means capital flows to or from Belarus, Kazakhstan, Russia and Ukraine driven by common interest in joint development of agribusiness and understanding of its prospects and specific features, and the close traditional economic ties.

Interregional cooperation and integration processes in agribusiness are stronger in border regions where joint processing ventures are located. For example, of the 27 regions of the Russian Federation bordering CIS countries, eleven border seven oblasts of Kazakhstan. Cross-border trade accounts for 70% of all trade between Kazakhstan and Russia.

The most important export item is grain; it is imported by the Russian regions. Kazakhstan is the second largest supplier of flour to the Russian market. On the whole, Kazakhstan's grain sector receives more than half of all investment in agricultural fixed assets. As a consequence of this, large Russian production and trading companies that have assets in Ukraine, Belarus and other CIS countries have shown interest in buying Kazakh assets with a view to founding large intraregional agribusiness companies. Kazakh players, in turn, have shown considerable interest in Russian agribusinesses. Kazakhstan has accumulated some positive experience of this type of cooperation. Nastyusha, a Russian company which produces, stores, processes and sells grain in Russia, Belarus, Kazakhstan and Lithuania, now owns 16 grain elevators, 12 farms with a total sown area exceeding 200,000 hectares, and a pig complex in Kazakhstan.

An example of similar Kazakh presence in Russian agribusiness is Ivolga Holding. This company is one of the top three Kazakh grain producers; it owns over 600,000 hectares of farm land in Russia and produces some 500,000 tonnes of grain (mainly 4 and 5 class wheat) in this country (Business Resource Central Asia, 2008). Ivolga Holding also owns more than ten elevators in Russia, and most of its assets are concentrated in Orenburg, Chelyabinsk and Kursk oblasts.

Most investment is being made in new farm machinery. Ivolga Holding is planning to launch the assembly of tractors jointly with the St. Petersburg Tractor Factory on the basis of its own Agrotekhmarsh facility. Other Kazakh players on the Russian market are Korporatsiya APK-Invest, Agrotsentr Astana LLP, and Zernovaya Industriya LLP. Their shares in the overall

production structure in Kazakhstan vary from 3% to 10%, and in Russia they mainly engage in grain storage, transshipment and processing.

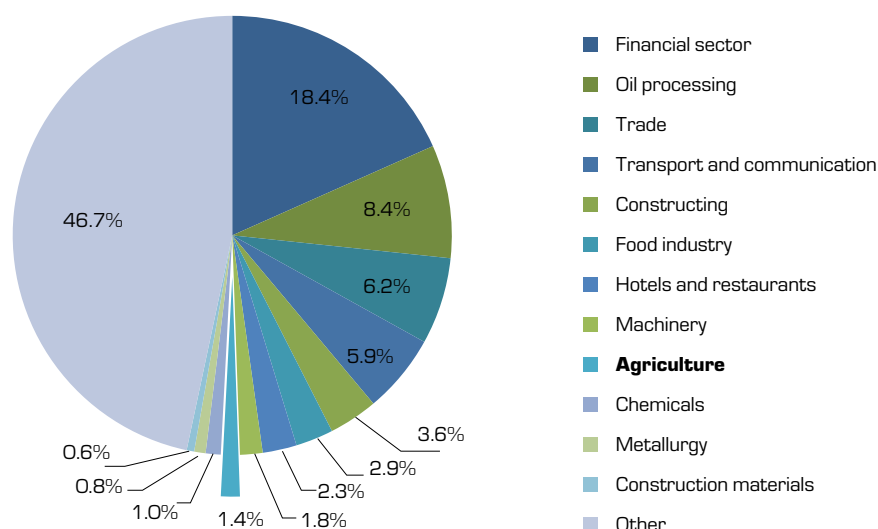
Another promising target for investment in Kazakhstan is livestock production, especially pasture husbandry, which, given skilful use of the vast pasture areas, would allow competitive and environmentally safe meat to be produced at a low cost.

Wimm-Bill-Dann Foods of Russia also showed an interest in the Kazakh milk producer FoodMaster when considering expansion in Central Asia³. However, preference was given to Bishkeksut of Kyrgyzstan, FoodMaster's main competitor in this market. Investing in Kyrgyzstan is clearly warranted by a number of the benefits that are offered by this country's investment climate, especially cheaper labour and raw materials in comparison with Kazakhstan. In addition, over 95% of Kazakh milk is produced by small farms and households; this production falls short of the demand and does not meet quality standards. These structural problems pose a serious barrier to foreign (e.g. from Russia) investment in the Kazakh milk and meat sector.

Our analysis of investment activities allows us to conclude that Russia is the main investor in the region. Large agribusiness holding companies from Russia have assets in Ukraine and Belarus. These two countries are the main recipients of Russian investment in the agricultural sector. In Ukraine joint ventures were established in the farm machinery industry: for example, Agromashkholding and the Ukrainian corporation UPEK founded a JV to manufacture Yenisey combine harvesters at the Lozovsky Combine Harvester Works. Some joint projects are being implemented at the Kharkov Tractor Works (Kovalenko, 2009). It should be stressed, however, that agriculture accounts for mere 1.4% in the structure of Russian investment in Ukraine (see Figure 2.2).

Figure 2.2.
The structure of Russian investment in Ukraine

Source:
the Statistics Agency
of Ukraine



The Russian investment company Unimilk also intended to expand its business into post-Soviet countries, but recently there was a shift of emphasis from Kazakhstan and Ukraine to Belarus where the Russian presence is still weak. In the summer of 2008 the Belarusian Ministry of Agriculture declared that a framework agreement will be made with Russian investors (particularly, Unimilk) on establishing a number of JVs in the livestock sector in Belarus. First of all, these will include projects on building new livestock complexes and reconstructing existing ones. Unimilk agreed to build a modern dairy plant in the Shklov District, Mogilev Oblast. The investors will also build or modernise a number of dairy plants in other regions of the country.

³ Unimilk and Danone also considered entering Central Asian markets by acquiring FoodMaster.

These projects will be implemented over four years; some of them are being financed since 2008. A special working group was established, all required authorisations were obtained, and a list of target assets in Belarus was made (Nikolayeva, 2008). The main objective for the Russian investors is to boost Belarusian livestock production and export it to Russia and other countries. According to the Belarusian Ministry of Agriculture, total Russian investment in the country's agricultural sector is estimated at hundreds of millions dollars.

According to official statistics, at present there are no significant investment flows from Russia to Kazakhstan. None of EurAsEC countries is on the list of the major sources of investment in Kazakhstan's agricultural sector (see Figure 2.3).

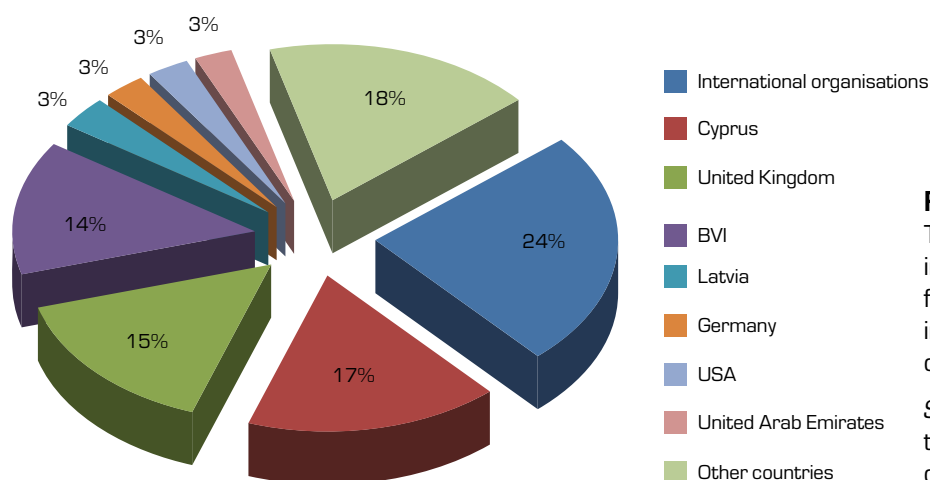


Figure 2.3.
The structure of foreign investment in agriculture, forestry, and fishing industry in Kazakhstan as of September 31, 2009

Source:
the National Bank of Kazakhstan

However, unofficial data suggest that the country's agricultural sector receives significant Russian investment via offshore jurisdictions. Kazakhstan itself is an active player in the region: in 2008 Kazexportastyk purchased a grain terminal in Kherson, Ukraine, in order to improve grain export infrastructure. Kazakh investors were also active in Russia: in 2006 TuranAlem and its Russian subsidiary, Slavinvestbank, acquired the Izumrud, Girkubs, Pavlovsky and Kanevsky sugar plants in the Krasnodar Territory from Karavai Plus (Taganrog, Russia). In 2003 TuranAlem's subsidiaries acquired control over the assets of the International Sugar Company which included four sugar plants and ten agribusiness companies (Heifetz, 2009). Finally, in 2006 in Dzerzhinsk, Nizhny Novgorod Oblast, VitaRos (a subsidiary of Kazakh VITA) launched a soy facility. In 2007 this facility produced and sold 10,000 tonnes of products (VitaSoy.kz).

2.3. The Problems and Prospects

At present mutual investment by EurAsEC countries is scarce due to a number of reasons: the low capacity of assets inherited from the Soviet economic system which do not meet modern productivity, safety and quality requirements; the increasing competition with producers from China, Turkey, South Korea, Japan, the UAE, the US, Canada and the EU which possess advanced technology and recognised brands; administrative interference; protectionist policies in foreign trade and investments; the problems associated with payments and cargo transportation, etc. The resolution of these problems is complicated by differences in the stakeholders' positions on some issues which require negotiations and the political will.

In crisis conditions, investing in agriculture appears to be a good choice because, unlike the products of any other industry, farm produce remains in demand at all times. On the whole, we can conclude that the current status of agribusiness in the countries under review is better than elsewhere, and foreign investment can provide an impetus for rapid development and modernisation of this sector.

The common tasks faced by the stakeholders will require joint organisational solutions, particularly:

- founding TNCs with assets located in several countries, which will serve as vehicles of mutually beneficial international cooperation. The creation of the Grain pool by Kazakhstan, Russia and Ukraine which will account for two-thirds of the total grain market would be an example of such cooperation (this initiative is discussed in more detail in section 4.1);
- exchange and co-ownership of valuable assets by member states;
- founding JVs with the participation of local public or private companies;
- launching production without merging assets;
- creating strategic alliances in individual economic sectors;
- holding periodic business and investment forums in regions with developed agribusiness.

The tasks listed above will require the modernisation of all integrating countries. The shift of emphasis to priority projects capable of catalysing structural changes in the economy and boosting the production of safe, high-value-added goods will ensure qualitative changes in relations and cooperation between CIS and EurAsEC countries.

At present, one of the main objectives of agrarian strategy is the reintegration of agribusiness of Russia, Kazakhstan, Ukraine and Belarus, as a precondition for enhancing the efficiency of production, collective food security, and sustained supply of farm produce to the population.

In order to become competitive players in global markets, the countries under review need to create a fully competitive environment within the CIS and take consistent measures against monopolistic trends in the agricultural sector. International experience shows that regional cooperation is more efficient and dynamic if it is driven by a powerful economic centre which promotes innovations: the United States in NAFTA, Germany and France in the EU, Brazil in MERCOSUR, Singapore in ASEAN, etc. The role of this centre in the CIS and EurAsEC belongs to Russia, as it is unmatched in terms of GDP, area, population number, and innovative and financial potential. An integration core may consist of a single country or a group of countries (e.g., the members of the Customs Union, as they have common economic and political interests).

2.4. Priority Targets for Mutual Investment

Apart from the development of the raw material base, modernisation and building of new, competitive processing facilities, there are some other targets for investment which are just as important for the creation of a healthy agricultural sector capable of providing real income for the state and the population.

In particular, the agricultural sector in Belarus, Kazakhstan, Russia and Ukraine offers the following investment opportunities:

- **Export infrastructure** for prompt response to changing conditions of agricultural markets and efficient product storage and delivery. Export infrastructure is a basic component of a competitive agricultural sector. The most cost-effective and fast delivery routes should be developed (especially for grain). The reduction of the transport component of export prices will help attract new customers and expedite product delivery to target markets; this, in turn, will allow proceeds to return to the sector quickly to replenish working capital. Therefore, although investing in transport infrastructure does not directly relate to agribusiness, in this paper we view transport infrastructure as an important element of agriculture development.

As we have mentioned above, the main importers of grain from the countries under review are European and Southeast Asian countries. The latter are the most promising markets, as they have no domestic grain production, whereas the increase in consumption forecast

by FAO and other international organisations will be especially pronounced in this region. Despite the potential of this market, the transport routes to Southeast Asia and the Persian Gulf are far from perfect: to date there is no multi-modal transport system. However, the countries under review are making an effort to improve the situation. Particular mention is due to the North–South international transport corridor — the decision to develop it was adopted in September 2000. This route connecting Russia and Ukraine with Southeast Asia (particularly, India) via Kazakhstan, Turkmenistan and Iran is the shortest and cheapest option for delivery of raw materials (grain, cotton from Tajikistan and oil products from Central Asia). However, at present this corridor is not used on its full capacity. In 2007 the port of Olya on the Caspian — the key cargo handling centre of the North–South corridor — shipped mere 435,000 tonnes of cargo, whereas the target set in 2000 was 3 million tonnes in five years (Vinokurov et al., 2009). This delay is attributable principally to the uneven pace of work to create the corridor. Iran and Russia have practically completed the construction or modernisation of their respective sections. Turkmenistan has built 150 km of the planned 477 km of railways; it is expected that the Turkmen section will be finalised by the end of 2011 (Emerson & Vinokurov, 2009). Kazakhstan lags far behind: the project has long been suspended at the feasibility study stage, and construction actually began in the 4th quarter of 2009. The efficient functioning of the corridor will require concerted efforts by all member states, and the latter have to accelerate the preparatory work.

Another important aspect of export infrastructure development is the creation of an extensive network of grain terminals. Uninterrupted delivery of exported products to end users should be secured despite the sharp market fluctuations. This can be achieved by building new grain elevators, terminals and storage facilities. These activities should not be confined to internal areas: the availability of grain terminals in the vicinity of sea ports is a precondition for fast and efficient shipment, as grain to Asian and European markets is delivered principally by sea. As we have mentioned above, Kazakhstan's Kazexportastyk acquired a grain terminal in Ukraine. This suggests that there is an understanding of the importance of investing in such assets. These efforts should be continued: grain terminals need to be constructed in other neighbouring (Turkmenistan, Georgia) and remote (Iran, the Baltic, India) countries.

- **Grain, meat and milk farms.** TNC investment in agriculture is especially important in the light of the need to modernise the sector. TNCs are in a position to introduce new technology, which can boost productivity and ensure compliance with applicable safety and quality standards. This in turn can improve the availability of products due to extensive production and distribution networks. TNCs also develop their own logistics systems which exclude their competitors and ensure optimal product distribution. To be able to compete with foreign companies on domestic (and, potentially, external) markets, CIS countries have to combine their efforts and make full use of the advantages provided by intergovernmental agreements within the CIS and EurAsEC frameworks for strengthening regional integration.

Eurasian TNCs successfully operate in other economic sectors in the countries under review and elsewhere. It is worth noting the telecommunications sector in which large TNCs (MTS, Vypelkom) are active throughout the region. Likewise, in our opinion, large holding companies such as Nastyusha or Ivolga would act as a consolidating power in the grain sector. In Kazakhstan, projects were commenced to create milk clusters and meat and milk mega-farms. For example, Alatau Dairy LLP and the Kazkommertsbank group (Meridian Capital LLP) are preparing a breakthrough project to launch milk production in Almaty Oblast (Smirnov et al., 2008). In the livestock sector, TNCs could be founded by large milk producers from Russia (Wimm–Bill–Dann, Unimilk, etc.) and meat processing companies from Ukraine and Belarus. Finally, another important area of activity for Eurasian TNCs is the food industry which produces high-value-added foods. In this sector, the role of consolidation centres would be played by large companies from Russia (Cherkizovo Group, Mikoyanovsky Meat

2. Mutual investment in agribusiness

Processing Plant, Razgulyai Group), Ukraine (Mironovsky Khleboprodukt, Astarta Holding, Kernel) and Kazakhstan (Vita, etc.).

- **Manufacture of farm machinery.** Farms in all countries under review are poorly equipped, and creation of JVs to manufacture modern farm machinery is a precondition to raising the competitiveness of agribusiness. The launch of the Customs Union of Belarus, Kazakhstan and Russia in 2010 is expected to assist the revival of domestic mechanical engineering. Another priority is the provision of preferential loans and introduction of financial leasing for purchasing farm machinery during the crisis. The sector needs not only crop harvesting machines (combine harvesters, tractors, etc.), but also equipment for processing grain and fodder, livestock farm and slaughter equipment (which is especially important giving the fact that slaughter is generally being made at home in inappropriate conditions), and equipment for processing grain, meat and milk into the final products with high value added.



3. Trade Integration in Agribusiness

3.1. Export and Import of Farm Produce by the Countries Under Review

Cereals (particularly, wheat) are the staple export of Kazakhstan, Russia and Ukraine — this can be explained by the enormous level of production that exceeds domestic demand. Russia, Ukraine and Kazakhstan are the world's largest grain exporters (ranking 6th, 7th and 8th, respectively). In 2000–2008s these three countries boosted their common cereals export potential from 6% to 24% of the world market. Notably, most experts believe that each of these three countries has its own niche on the world wheat market: Ukraine mainly exports forage wheat; Russia exports 4th class wheat; and Kazakhstan's higher grade wheat is used to make blends. Grain is exported mainly to the EU, South Asia and North Africa. Producers from these three countries have developed close ties with their main buyers and trade of grain on global and regional commodity exchanges.

Grain export demonstrated sustained growth during the past decade, and so did the export of grain processing products. In 2008 Kazakhstan became the world's largest supplier of flour, an achievement that had a positive economic effect: the added value generated by grain processing was retained by the domestic economy. According to preliminary estimates for 2009, Kazakhstan retained its leading position (2.2 million tonnes of flour were exported in January–December 2009).

A portion of grain produced by the countries under review is supplied to other CIS countries. This can be explained by the geographic proximity and traditionally extensive trade ties of the region's countries inherited from the Soviet epoch. The largest importer of cereals in the CIS is Azerbaijan. Notably, in the CIS context, Belarus is one of the top three importers of cereals grown in Kazakhstan, Russia and Ukraine: its own production of 7 million tonnes falls short of domestic demand. As a result, Belarus imports 400,000–500,000 tonnes of cereals from other CIS countries annually (see Table 3.1).

Importer countries	Import from CIS countries, total	Including importer countries									
		Azerbaijan	Armenia	Belarus	Georgia	Kazakhstan	Kyrgyzstan	Moldova	Russia	Tajikistan	Ukraine
Azerbaijan	1406	–	–	–	0.0	484	–	2	767	–	154
Armenia	360	–	–	–	3	39	–	–	275	–	43
Belarus	409	–	–	–	–	64	–	3	101	–	242
Georgia	–	–	–	–	–	–	–	–	–	–	–
Kazakhstan	103	0.01	0.01	–	–	–	–	0.0	75	–	28
Kyrgyzstan	311	–	–	–	–	297	–	–	11	–	3
Moldova	39	–	–	–	–	14	–	–	7	–	18
Russia	583	–	–	0.8	–	261	–	0.02	–	0.0	321
Tajikistan	274	–	–	–	–	255	0.05	–	16	–	3
Turkmenistan	–	–	–	–	–	–	–	–	–	–	–
Uzbekistan	–	–	–	–	–	–	–	–	–	–	–
Ukraine	11	–	–	0.4	–	6	–	–	4	0.02	–

Table 3.1.

Import of cereals from CIS countries in 2008 according to importer country's statistics ('000 tonnes)

Source: CIS Statistics Committee

Trade in cereals in the region has great potential, but the trading process itself is inefficient due to the lack of transparency in pricing. In line with this, in the beginning of 2009 Kazakhstan and Russia — the largest cereals producers in the region — founded the Eurasian Trading System (ETS) in order to optimise grain trading operations. Almost 60% of the shares in ETS is owned by RCS of Russia and 40% by RFCA of Kazakhstan. The establishment of this Russian–Kazakh commodity exchange exemplifies efficient integration of commodity markets. At present, the main products traded on ETS are grain and flour (90%).

3. Trade integration in agribusiness

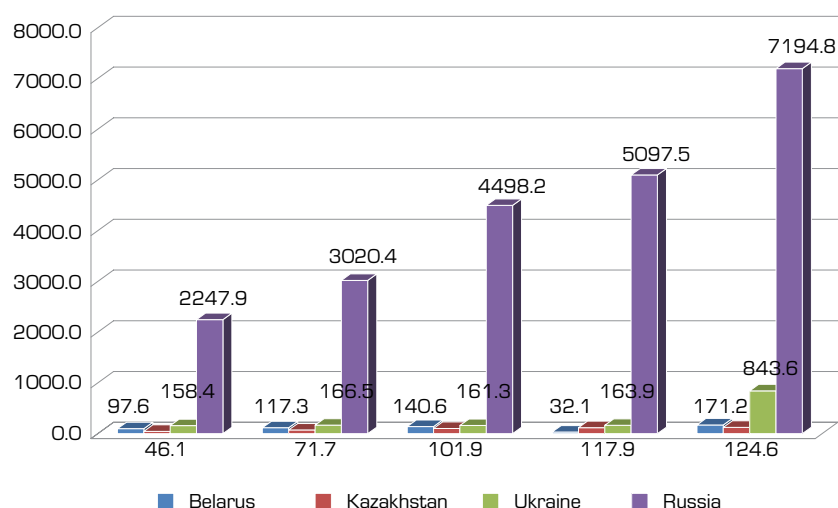
It is expected that granting small and medium size farms access to the trading floor will enable them to sell grain directly to end users, and both parties will benefit from the direct sale mechanism. In addition, Kazakh commodity markets will become more attractive to international traders and investors. To date, ETS's customers include companies from Kyrgyzstan, Uzbekistan, Iran and Turkey, apart from Kazakh and Russian traders (Nurtazina, 2009). The first trading session on ETS took place on March 30, 2009.

Although trade in cereals was rather sluggish in the first months, by the end of 2009 ETS achieved good results. Sales on ETS from March 30 to December 31, 2009 totalled \$403.8 million⁴, or 2,650,246 tonnes of grain, which is 13.5% of Kazakhstan's total production (KazInform, 2009). In future, the development of commodity exchanges in Kazakhstan is expected to boost grain sales on ETS even further. This, however, will require a sound awareness policy aimed at grain producers and governmental support for civilised trade and transparent pricing.

The status of the meat and milk markets in four countries under review is the complete opposite. Almost all meat and meat processing products are imported (see Figure 3.1), the main suppliers being the Americas and the EU.

Figure 3.1.
Dynamics of imports of meat
to Belarus, Kazakhstan, Russia
and Ukraine (\$ mln)

Source:
UNCTAD international trade
database



In other words, Belarus, Russia, Kazakhstan and Ukraine are essentially net importers. Practically all exports from these countries enter CIS markets. Kazakhstan, Russia and Ukraine all demonstrate strong potential for the development of poultry export. For Belarus, the most promising exports are meat and by-products. To this end, concerted efforts need to be made and common conceptual approaches to the development of meat production and export need to be formulated in order to prevent mutual competition.

With the exception of Belarus, the countries under review are leading grain exporters. The strong competitive position of this product on the global market and favourable market conditions resulting from the population growth in China and India, improvements in living standards in these and other developing countries, and an increase in consumer demand have assisted the development of the grain sector globally. The export of livestock products from the countries under review is confined to CIS markets, which indicates that the meat and milk sector needs significant reforms. In the livestock sector, the most promising positions are held by Belarus (meat) and Ukraine (milk products), and this fact should be taken into account when formulating common conceptual approaches.

⁴ At the exchange rate set by the National Bank of Kazakhstan on January 12, 2010.



The export of poultry products is demonstrating rapid growth, as it offers quicker payback for investors. The pace of development of poultry export by Russia, Kazakhstan and Ukraine exceeds that of global import. At the same time, domestic demand in these countries is mainly satisfied by imported products. The fact that export is not diversified and is limited to CIS markets is the main barrier to the expansion of production: productivity in the sector is decreasing, the cost of the product is becoming higher, and its competitiveness is deteriorating. As a result, domestic markets have become flooded with cheaper imports. A lack of coordination in export and import and mutual competition negate the advantages of new technology adopted in the sector.

The grain market is adequately diversified, and three countries out of the four — Ukraine, Russia and Kazakhstan — are among the world's top grain exporters. The demand for farm produce resulting from population and consumption growth in India, China and other rapidly developing countries, as well as globalisation and urbanisation will increase. The consumption of cereals will also increase due to the spread of eco-fuel and new food preferences. According to the International Food Policy Research Institute (IFPRI), by 2015 global demand for grain will increase by 20% (von Braun, 2007). An increase in global consumer demand leads to an increase in export. The removal of barriers to mutual trade and transportation and a coordinated policy of entering external markets will enable Ukraine, Russia and Kazakhstan to boost their grain export.

The sales of organic (environmentally safe) products grew from \$19 billion in the EU, the US and Japan in 2001 to \$35 billion in 2005. A particular feature of this market segment is its sustained growth (10–20% annually). Kazakhstan and Russia are potential exporters of some of these products, as they have better environmental conditions, large tracts of unused farmland and cheap workforce. These advantages coupled with high world prices make organic products lucrative exports with products that can be developed in crop and livestock production. However, to protect this market, environmental production standards and an accredited certification system need to be introduced. Therefore, these countries face the task of creating a harmonised legal framework for certification and marking and make it recognised by international trade partners, which will enable them to remove technical barriers to export in accordance with WTO requirements.

3.2. A Review of Trade in Cereals in the EDB's SIEI

Since the objective of this paper is to provide an insight into sectoral cooperation of the countries under review, an analysis of integration in trade in grain — the basic farm product — is

the logical continuation of the discussion of the agricultural markets in these countries. The EDB developed the System of Indicators of Eurasian Integration (SIEI), which is intended as a tool for monitoring and assessing regional integration in the post-Soviet world (EDB, 2009). In the SIEI, trade in cereals is used among other indices. We will use this unique monitoring system to identify the main centres of agriculture integration in the countries under review.

The SIEI studies trade in cereals between CIS country pairs, between individual countries and integration groupings, and between integration groupings.

The analysis shows that the leader in agriculture integration of country pairs (based on data on cross-border trade in cereals, see Table 3.2) in the post-Soviet space is Kazakhstan. This country is present in all three leading country pairs: Kazakhstan–Azerbaijan, Kazakhstan–Turkmenistan and Kazakhstan–Kyrgyzstan. Trade in cereals by other CIS countries is not nearly as significant, in relation to their economy size. Most country pairs have no mutual trade in cereals at all.

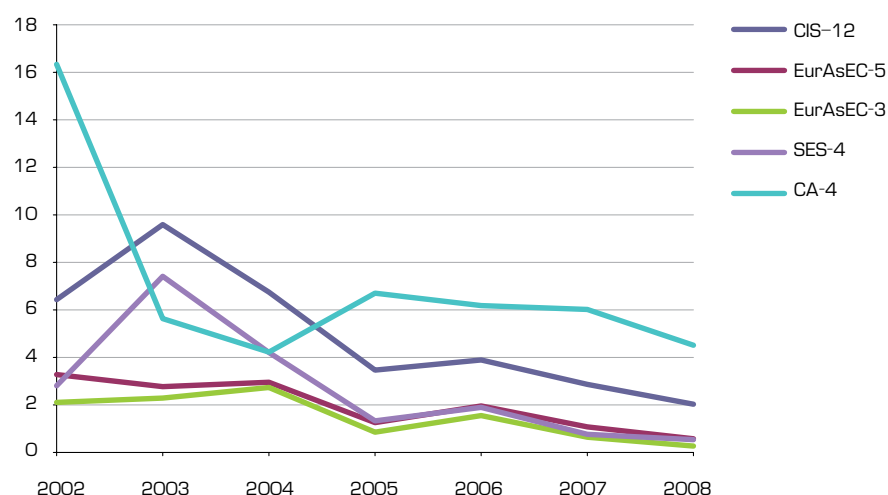
Kyrgyzstan is the leader in integration with CIS-12, which appears to be caused by the large volume of cereals export in relation to its economic size. Tajikistan ranks second. A similar structure is observed in the other four integration cores. The lowest levels of integration with CIS-12 and other groups are demonstrated by Russia, due to its enormous economy and powerful agricultural sector.

As with energy integration, trade in cereals in the post-Soviet space lags far behind the growth of national economies. This trend persisted despite the assumed improvement in the quality of statistics. In 2002–2008, the agriculture integration index increased only in the Kazakhstan–Turkmenistan country pair. Turkmenistan is also the only country that demonstrated an increase in the levels of agriculture integration with all the five groupings during the reporting period.

An analysis of integration within the frameworks of the five groupings (see Figure 3.2) also confirms that integration levels were declining during the seven-year period. At the same time, the development trends were less stable than those of other indices. For example, in CA-4 the integration index stabilised after a decline in 2003 at a fairly high level that exceeds the levels of the other groupings.

Figure 3.2.
The dynamics of agriculture
integration in the five
post-Soviet groupings

Source:
EDB (2009: 22)



Therefore, we can conclude that among the countries under review Kazakhstan is the integration leader in terms of trade in cereals. Within time, four countries become less integrated as a result of the trade expansion to remote markets which are deficient in grain. However, it should be noted that CIS countries will remain permanent buyers of grain from Russia, Kazakhstan and Ukraine, due to their geographic, political and cultural proximity, hence, trade integration within the CIS is the long-term phenomenon.

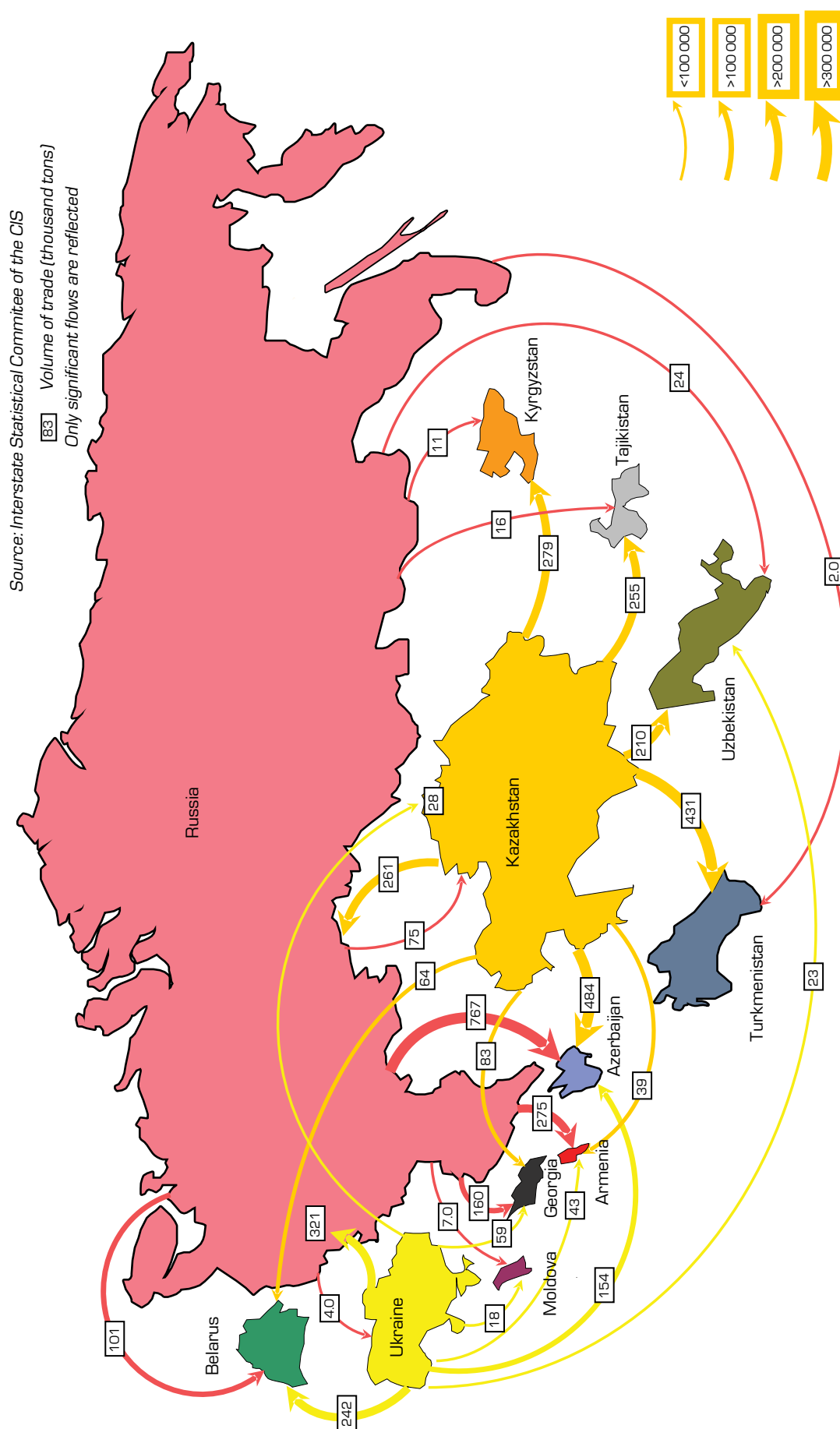


Figure 3.3.
Trade in cereals between CIS countries in 2008
Source: EDB (2009: 73)

Country pair	2002	2003	2004	2005	2006	2007	2008
From Russia to Azerbaijan	188.0	191.0	532.0	853.0	679.0	507.0	767.0
From Russia to Armenia	259.0	54.0	272.0	302.0	298.0	385.0	275.0
From Russia to Belarus	494.0	360.0	207.0	64.0	67.0	118.0	101.0
From Russia to Georgia	111.0	132.0	151.0	290.0	403.0	446.0	160.0
From Russia to Kazakhstan	13.0	21.0	2.0	27.0	66.0	73.0	75.0
From Russia to Kyrgyzstan	0.2	0.0	0.8	0.0	0.1	3.0	11.0
From Russia to Moldova	0.8	97.0	0.7	0.7	0.2	10.0	7.0
From Russia to Tajikistan	8.0	3.0	0.3	5.0	8.0	3.0	16.0
From Russia to Turkmenistan	1.0	0.0	0.1	0.0	0.0	1.0	2.0
From Russia to Uzbekistan	2.0	0.9	0.2	0.2	2.0	4.0	24.0
From Russia to Ukraine	5.0	1 074.0	183.0	10.0	25.0	9.0	4.0
From Kazakhstan to Azerbaijan	462.0	650.0	446.0	109.0	367.0	955.0	484.0
From Kazakhstan to Armenia	4.0		38.0		3.0	48.0	39.0
From Kazakhstan to Belarus	40.0	12.0	41.0	21.0	110.0	213.0	64.0
From Kazakhstan to Georgia	20.0	8.0	79.0	27.0	103.0	198.0	83.0
From Kazakhstan to Kyrgyzstan	165.0	96.0	72.0	137.0	218.0	357.0	297.0
From Kazakhstan to Moldova		49.0	18.0		3.0		14.0
From Kazakhstan to Russia	260.0	704.0	1 543.0	612.0	1 472.0	519.0	261.0
From Kazakhstan to Tajikistan	285.0	141.0	85.0	206.0	234.0	272.0	255.0
From Kazakhstan to Turkmenistan	6.0	1.0	0.4	0.0	2.0	133.0	431.0
From Kazakhstan to Uzbekistan	134.0	11.0	31.0	68.0	136.0	158.0	210.0
From Kazakhstan to Ukraine	37.0	1 536.0	395.0	0.7	0.8	10.0	6.0
From Ukraine to Azerbaijan	2.0	2.0	8.0	3.0	6.0	1.0	154.0
From Ukraine to Armenia	38.0	14.0	35.0	6.0	19.0	41.0	43.0
From Ukraine to Belarus	242.0	61.0	230.0	295.0	302.0	205.0	242.0
From Ukraine to Georgia	4.0	1.0	8.0	17.0	61.0	38.0	59.0
From Ukraine to Kazakhstan			0.6	3.0	0.5	0.2	28.0
From Ukraine to Kyrgyzstan	0.3						3.0
From Ukraine to Moldova	2.0	4.0	4.0	1.0	3.0	2.0	18.0
From Ukraine to Russia	104.0	136.0	433.0	209.0	257.0	59.0	321.0
From Ukraine to Tajikistan	0.1				0.0		3.0
From Ukraine to Turkmenistan							
From Ukraine to Uzbekistan	0.3			0.3	0.1	0.3	23.0
From Belarus to Azerbaijan							
From Belarus to Armenia							
From Belarus to Georgia							
From Belarus to Kazakhstan							
From Belarus to Kyrgyzstan							
From Belarus to Moldova		0.7				0.1	
From Belarus to Russia	3.0	2.0	7.0	4.0	4.0	0.7	0.8
From Belarus to Tajikistan							
From Belarus to Turkmenistan							
From Belarus to Uzbekistan							
From Belarus to Ukraine		25.0	1.0	0.2		0.1	0.4
From Moldova to Azerbaijan						2.0	
From Moldova to Armenia	3.0	0.8	3.0			0.2	
From Moldova to Belarus	20.0	11.0	12.0	15.0	15.0	15.0	
From Moldova to Georgia				3.0	5.0		
From Moldova to Kazakhstan	0.0			0.0	0.0	0.0	
From Moldova to Kyrgyzstan	0.0	0.0		0.0			
From Moldova to Russia	3.0	0.5	0.8	0.4		0.0	
From Moldova to Tajikistan							
From Moldova to Turkmenistan							
From Moldova to Uzbekistan				0.0	1.0	0.1	
From Moldova to Ukraine	2.0	2.0	22.0	53.0	45.0	34.0	
From Kyrgyzstan to Azerbaijan							
From Kyrgyzstan to Armenia							
From Kyrgyzstan to Belarus			0.2				
From Kyrgyzstan to Georgia						0.1	
From Kyrgyzstan to Kazakhstan	0.1	0.1		0.0			

Table 3.2.
Mutual trade
in cereals
in the CIS
(’000 tonnes)

Source:
CIS Statistics
Committee

From Kyrgyzstan to Moldova						
From Kyrgyzstan to Russia	0.0	0.7		0.0	0.0	
From Kyrgyzstan to Tajikistan	1.0				0.0	0.1
From Kyrgyzstan to Turkmenistan	0.0				1.0	
From Kyrgyzstan to Uzbekistan	0.0					
From Kyrgyzstan to Ukraine						
From Azerbaijan to Armenia						
From Azerbaijan to Belarus						
From Azerbaijan to Georgia	0.5	2.0	4.0	1.0	0.6	1.0
From Azerbaijan to Kazakhstan				0.0	0.0	0.0
From Azerbaijan to Kyrgyzstan						
From Azerbaijan to Moldova						
From Azerbaijan to Russia		1.0				
From Azerbaijan to Tajikistan						
From Azerbaijan to Turkmenistan						
From Azerbaijan to Uzbekistan						
From Azerbaijan to Ukraine						
From Armenia to Azerbaijan						
From Armenia to Belarus						
From Armenia to Georgia	0.0			4.0		0.0
From Armenia to Kazakhstan						0.0
From Armenia to Kyrgyzstan						
From Armenia to Moldova						
From Armenia to Russia	0.0					0.0
From Armenia to Tajikistan						
From Armenia to Turkmenistan						
From Armenia to Uzbekistan						
From Armenia to Ukraine						
From Tajikistan to Azerbaijan						
From Tajikistan to Armenia						
From Tajikistan to Belarus						
From Tajikistan to Georgia						
From Tajikistan to Kazakhstan						0.0
From Tajikistan to Kyrgyzstan						
From Tajikistan to Moldova						
From Tajikistan to Russia			0.1	0.1		
From Tajikistan to Turkmenistan						
From Tajikistan to Uzbekistan						
From Tajikistan to Ukraine						0.0
From Uzbekistan to Azerbaijan		163.0	0.0	3.0	3.0	
From Uzbekistan to Armenia		39.0	8.0			
From Uzbekistan to Belarus		3.0				
From Uzbekistan to Georgia		68.0				
From Uzbekistan to Kazakhstan		5.0	0.0		0.0	
From Uzbekistan to Kyrgyzstan		18.0	25.0	9.0	8.0	
From Uzbekistan to Moldova		0.6				
From Uzbekistan to Russia		13.0	0.3			
From Uzbekistan to Tajikistan	1.0	0.8	41.0	74.0	44.0	12.0
From Uzbekistan to Turkmenistan						
From Uzbekistan to Ukraine		4.0	0.1			
From Georgia to Azerbaijan				0.0		
From Georgia to Armenia	40.0	72.0	4.0	0.1	70.0	3.0
From Georgia to Belarus						
From Georgia to Kazakhstan						
From Georgia to Kyrgyzstan						
From Georgia to Moldova						
From Georgia to Russia		1.0	11.0			
From Georgia to Tajikistan						
From Georgia to Turkmenistan						
From Georgia to Uzbekistan						
From Georgia to Ukraine			8.0			

4. Regional Integration Initiatives in Agribusiness

The trade integration of Belarus, Kazakhstan, Russia and Ukraine is necessitated by the following reasons:

- Most importantly, agribusiness in these countries has strong competitive advantages in regional and global markets. At present, these advantages are more pronounced in grain production and less in the livestock and foods sectors. We believe that making full use of these advantages will require cooperation in production and transportation. In economic terms, isolated development of agribusiness in each of these countries is a sub-optimal solution.
- The historic specialisation of these countries in certain products (the competitive advantages of hard wheat production in Kazakhstan, Russia and Ukraine, sugar production in Ukraine, pork, beef and lint production in Belarus) offers great potential for trade within the sector.
- Common use of the transport infrastructure inherited from the Soviet Union which is capable of supporting intensive flows of farm production and foods will enable these countries to boost agribusiness output and raise living standards.
- The agricultural markets of Belarus, Kazakhstan, Russia and Ukraine are institutionally similar, which can be explained by their common economic and political past. This warrants mutual investment and institutional integration.

In our opinion, sectoral integration in agribusiness is an efficient tool for the removal of barriers to trade and the enhancement of the competitiveness of domestic farm produce. Realising this fact, Belarus, Kazakhstan, Russia and Ukraine signed a number of documents on joint development of agriculture. This applies to two agreements made in the first half of 2009: on establishing the Grain pool, and Customs Union countries' joining the WTO in a coordinated manner.

4.1. The Grain Pool

In recent years global commodity exchanges saw swift fluctuations in grain prices resulting from changes in production volumes. In 2008, a bumper harvest coupled with the economic crisis resulted in a dramatic drop in prices, occurring after a steady growth during the previous years. Ukraine, Russia and Kazakhstan responded to these fluctuations by organising government intervention and procurement which allowed adequate grain prices on regional markets to be maintained. However, these measures were poorly coordinated and could not halt the fall in prices. This indicates that a well-coordinated policy of these three large players on the grain market is essential for enhancing the competitiveness of their exports.

In addition, the strong potential of these grain exporters is undermined by the fact that, due to their geographic position, natural and climatic conditions, as well as historic and cultural ties their exports enter the same markets at the same time, and using the same transport infrastructure. As a result, national exporter companies compete toughly with each other rather than with foreign suppliers. This renders their efforts inefficient and reduces their chances of strengthening their positions on global markets. According to experts, Russia, Kazakhstan and Ukraine lose \$10–\$20 on each tonne of grain as a result of mutual competition (Mosyakin, 2009). The intention of each of these states to create a separate export infrastructure reduces the efficiency of investment. Therefore, realising their export potential and strengthening their positions in global grain markets will require concerted efforts, a common export policy, and a vehicle for implementing it.

When exporting grain, Ukraine suffers from a lack of elevators, Russia and Kazakhstan face logistical problems, and all the three countries have a common problem in the obsolescence



of their railway car fleet. Any future efforts to increase export will inevitably face the need to solve infrastructure problems which are already expected to complicate export transshipment in the near future. These problems require concerted efforts by and a coordinated investment policy from Ukraine, Russia and Kazakhstan aimed at developing infrastructure for the export of grain to the target markets. In other words, sectoral integration at the level of exporting countries will become an efficient mechanism for winning larger shares in global grain markets and increasing these countries' export revenue. In this context, establishing the Grain pool will be beneficial to all stakeholders, and its optimal functioning will only be possible if three states formulate a common export policy. Russia and Kazakhstan need the pool in order to enter global markets via Ukraine's ports, and the latter needs the pool to generate profit from transit.

At the World Grain Forum in St. Petersburg in June 2009 the representatives of the ministries of agriculture of Kazakhstan, Russia and Ukraine announced their intention to create a Grain (wheat) pool. This initiative had been discussed over the previous 2–3 years, and a working group was finally appointed and tasked with formulating the rules of the newly created organisation. The mass media hurriedly entitled this initiative "the grain OPEC". So, what are its underlying principles and prospects?

As we have stressed earlier, the three largest Eurasian grain exporters need to cooperate and jointly develop a common export policy. A large conglomerate having a considerable share in the global market will be in a position to control the pricing of grain, primarily wheat, and jointly use and develop the existing infrastructure. During the financial crisis the pool will function as a vehicle to merge the stakeholders' production and logistical potential and level the quality of their wheat, thus allowing them to save on expensive infrastructure projects.

In our opinion, the establishment of this "club" is a form of mutually beneficial cooperation: jointly these large players can multiply their export potential and make pricing predictable and controllable. In addition, the stakeholders will be able to implement their plans to raise joint cereals production to 225–250 million tonnes. According to experts, in 2–4 years the Ukrainian Black Sea ports alone will allow up to 42 million tonnes of Ukrainian and transit grain to be transhipped (Feofilov, 2009).

This initiative is an example of efficient integration at an industry level that could dramatically improve the position of certain Eurasian countries on grain markets. However, the Grain pool is yet to be created, and there are some serious doubts about Kiev's stance: although the benefits of this initiative for Ukraine are obvious, it is strongly opposed by the EU. A week after

the announcement of the establishment of the pool the EU Commissioner for Agriculture said that the EU disapproves of Ukraine's participation in these negotiations (Golubeva, 2009).

Therefore, it is not possible to forecast the start-up time of "the grain OPEC" (and whether it will be created at all). The process will be complicated by political pressure: the EU will not welcome the emergence of a new powerful and influential player and competitor. In addition, the Grain pool may face resistance from large grain importers concerned about cartelisation of supplies. In October 2009 the President of the Russian Grain Union even announced that Ukraine had abandoned its intentions declared in June 2009 under the EU's pressure (Mosyakin, 2009). Although the Ukrainian Ministry of Agriculture disavowed this statement, the unclear position of Kiev appears to be the main obstacle to the creation of the Grain pool. As we have stressed above, the optimal functioning of the pool will require participation of all the three countries; should Ukraine withdraw, the benefits for Kazakhstan and Russia will be negated.

On the whole, there are three possible scenarios, and each of them essentially depends on Ukraine's behaviour. Under the *optimistic* scenario, Kiev will realise that, despite its aspiration to assimilate into Europe, it should prioritise national interests and benefits. In this case the process will be smooth and "the grain OPEC" would be launched as early as 2010.

The opposite (*pessimistic*) scenario is also very likely. If Kiev's pro-European sentiment and continued pressure from the EU outweigh the desire to fully benefit from Ukraine's staple export, the process may be frozen, and the Grain pool may well remain another good idea on paper. There is also the *moderate* scenario, however: Ukraine's contradictory desire to secure its national interests (which are in line with those of its Eastern partners) and please the EU will delay the creation of the pool for years.

At this stage it is difficult to say which scenario is more likely. The course of events will depend on political factors, and these can change swiftly. Judging by the recent revival of discussions about the prospects of the Grain pool, the fate of this integration initiative can be decided in the next few months.

4.2. A Coordinated Policy for Joining the WTO

The most important barrier to agriculture development in the CIS is government support to the sector in developed countries. This problem is especially pronounced in livestock and milk production. The agricultural lobby in the US and Europe is very influential. As a result of government subsidies in various forms, the prices of farm produce from the US and the EU are much lower — despite the fact that the actual cost of this produce is much higher.

Annual government spending to support agriculture in the US and the EU is \$65 billion and €124 billion, respectively. Similar allocations in Russia, even given the comparable production volumes, are no match for these figures: mere \$170 million (Soyuz.By, 2008). In Belarus, Kazakhstan and Ukraine these figures are even smaller.

In addition to direct support for agribusiness in the form of export subsidies and numerous preferences, the EU and the Americas apply various protectionist policies. For example, in order to restrict access to the domestic market for producers from developing countries (which so far include the countries under review), the government may introduce quality standards which the latter cannot meet. The mechanism of restricting import on account of anti-dumping investigations is also widely used. In many cases developed countries simply impose direct barriers. This situation may become even worse after CIS countries join the WTO. For example, in October 2008 the European Commission introduced high customs duties on grain import from Ukraine (a WTO member since 2008) for two years, which is effectively a ban on grain import to the EU.

Issues relating to support for agriculture are hotly discussed during negotiations with the main trading partners including the US and the EU. One of the preconditions to joining the

WTO for the region's countries is the reduction of direct government support to agriculture and total transition to the "green basket"⁵. Another debated issue is the protection of domestic producers in the form of quotas on products supported by Western countries. These negotiations are characterised by pressure from developed countries and the wide application of the policy of unilateral concessions as a measure to accelerate joining the WTO. As a result, "small" economies such as Belarus and Kazakhstan are often forced to accept terms which can cost them irreparable damage to their domestic agricultural sector.

If a country joins the WTO on these terms, it must open its internal market for imports, whilst the developed countries do not do the same. This may put an end to that country's efforts to make its domestic production competitive. Therefore, it is critical to secure national interests at the negotiations stage and make full use of coordinated joining of the WTO, applying common approaches and securing support from major economic and political players; in our region that player is Russia. This will improve the chances of achieving satisfactory results and mutually beneficial liberalisation of trade.

In June 2009 *Belarus, Kazakhstan and Russia* announced their decision to suspend all negotiations over joining the WTO as individual countries and join that organisation as a *single customs territory* — integration initiative that directly influences agribusiness.

The integration process in EurAsEC is steadily moving towards its basic goal — the Customs Union of Belarus, Kazakhstan and Russia with prospective expansion by admitting other EurAsEC countries (Kyrgyzstan and Tajikistan). The unification work was officially started on January 1, 2010. Belarus and Russia had been negotiating joining the WTO individually since 1993 and Kazakhstan since 1996. Their decision to join the WTO as an integration grouping will set a precedent (this is the first such case in the history of the WTO and GATT) and provide a number of tangible advantages to the members of the Customs Union, especially Belarus and Kazakhstan. Joining the WTO together with a major economic and political player such as Russia will enable Astana and Minsk to secure more beneficial terms and fair mutual concessions during negotiations. The developed countries will have to deal with a regional grouping which accounts for 3.7% of global GDP, 3.1% of global exports and 2% of global imports.

In addition, given a fair balance of national interests within the Customs Union, this grouping will be able to make a positive effect on those economic sectors in its member states which especially need governments support — primarily, agribusiness.

However, the advisability of this joint step by Belarus, Kazakhstan and Russia must be carefully weighed, as it will delay the process of admitting each of these individual countries for several more years. According to Belarusian authorities, repeating the entire negotiation process may take twelve or more years (Manenok, 2009). This is a serious consideration, as Russia has practically completed its individual negotiation process (to 95%), and Kazakhstan was nearing completion (70%). This could be too high price for these three countries for an attempt to receive maximum advantages from WTO membership.

In any case, concerted efforts by Belarus, Russia and Kazakhstan as members of a large trading grouping with common interests will not be in vain: even at the current stage of joining the WTO individually, they have to develop common approaches towards agribusiness and other sensitive sectors. In this context, the official statement in October 2009 that Belarus, Kazakhstan and Russia will recommence negotiations over joining the WTO as individual countries, but in *close coordination* with each other (RIAN, 2009) indicates an optimal scenario that will allow them to accelerate the joining process while protecting their common interests.

⁵ "Green basket" means spending on programmes that do not directly relate to production or trade. These may include crop insurance, consulting and information support in rural areas, modernisation of rural infrastructure, research, investment subsidies, veterinarian services, etc.

5. Conclusion

This sector report focuses on challenges faced by agribusiness in Belarus, Kazakhstan, Russia and Ukraine and the ability of regional integration to mitigate the most urgent of them.

Mutual investment in agriculture can assist the transfer of technology, substitute government support (which is not always desirable in the context of global liberalisation), promote infrastructure and production development, and eventually provide benefits for all stakeholders.

Any regional initiatives of sectoral integration (the Grain pool, the Customs Union or joining the WTO in a coordinated manner) also assist the development of competitive agribusiness in the countries under review.

The integration aspect of agriculture development, particularly, encouraging mutual investment in this sector, is a new and poorly understood facet of the problem. This lack of understanding is largely attributable to the difficulty in obtaining reliable statistics on mutual investment and related trends. This report merely brings to light some facts relating to sectoral integration, which deserves further scrutiny.

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Contacts

Mr. Vladimir Yasinskiy

Member of the Executive Board,
Head of Strategy and Research Department, EDB
E-mail: yasinskiy_va@eabr.org
Telephone: +7 (727) 244 68 75

Mr. Evgeny Vinokurov

Ph. D., Deputy Head of Strategy and Research Department,
Head of Economic Analysis Division, EDB
E-mail: vinokurov_ey@eabr.org
Telephone: +7 (727) 244 40 44, ext. 6146

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