NEWSLETTER
Issue No. 24 | July - August 2014

The economic impact of Russian trade sanctions

In 2013, more than one quarter of Moldovan export revenues originated from Russia. Currently, Russia uses this economic leverage to exercise pressure on Moldova through a number of trade restrictions. Already since September 2013, an import ban for Moldovan wine is in place. In July 2014 additional import bans on meat and various kinds of fruit were introduced. Furthermore, the tariff rates for 19 types of goods were raised recently. This leads to the question to what extent these restrictions threaten the stability of the Moldovan economy.

Despite a drop in exports to Russia by almost one quarter during the first half of this year (compared to the same period last year), total Moldovan exports grew by 3% over the same period. However, the costs are likely to rise due to new restrictions which came into force in the mid of 2014. We estimate that the new and existing measures together could reduce export revenues by USD 145 m per year. This is equivalent to 25% of exports to Russia and to about 2% of Moldovan GDP. Thus, while the measures have the potential to reduce economic output; economic stability should not be threatened, provided there is an adequate policy response.

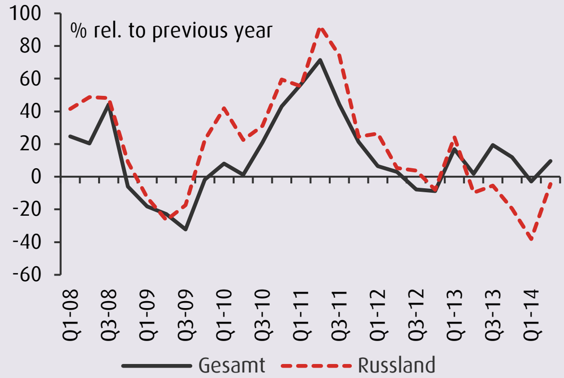
Importance of the Russian market

With a value of USD 632 m in 2013, exports to Russia play an important role for the Moldovan economy. In 2013 26% of total exports were sold to Russia. Therefore it is of no surprise that Russia uses trade restrictions to put pressure onto the Moldovan government. While this method is not new, the number and extent of the restrictions have significantly increased since the ratification of the Association Agreement. By now, a wide range of measures exists to prevent or hamper the export of Moldovan goods to Russia. Mainly the restrictions consist of import stops for three product categories: Wine, meat products and fruits. As an additional measure, Russia raised the import tariff rates for 19 types of products (mostly agricultural goods, food and also furniture). This leads to the question: What economic impact can be expected from the trade restrictions?

Consequences up to now

So far, a drop in Moldovan exports has not yet materialised. In fact, total exports even grew by 3% in the first half of 2014 compared to the same period of the previous year. In contrast, Moldovan exports to Russia plummeted by 24% in the first six months of this year. Hence, despite the reduction in exports to Russia, the total exports are so far only moderately affected as other geographic markets have compensated the decline. However, most of the trade restrictions have only come into force recently. For this reason, it should be examined whether the new measures have the potential to reverse export growth and whether this would threaten macroeconomic stability of Moldova.

Moldovan exports



Source: www.statistica.md

Expected impact of the restrictions

We assessed what direct impact of the existing and the newly announced trade restrictions can be expected on the Moldovan economy. In particular, we estimated the loss in export revenue in case the restrictions will remain in place for a period of one year. We base the estimations on trade data from the year 2013.

Already since September last year, the import of Moldovan wine and spirits has been banned. The ban, which the Russian consumer protection agency justified on health and safety grounds, is very effective: In the first half of the year 2014, total exports of the product group beverages (of which wine makes up the largest share) declined by one third compared to the same period of the previous year.

If this ban were to remain in place during the whole year, we expect a decrease in export revenues for wine and spirits of USD 45 m.

Since the beginning of July, the Russian consumer protection agency also stopped the import of certain meat products from Moldova. Among the products affected, the most relevant – from an economic point of view – is the export of beef. In 2013, meat with a total value of USD 17 m was exported to Russia. This is also the expected annual costs if the import ban remains in force during the whole year. In comparison to meat products, the agricultural sector of Moldova is more seriously affected by the import ban on fruits, which also came into force in July. The import ban targets apples, pears, peaches, plums and some other less important kinds of fruit. The timing of the import ban is especially damaging for the Moldovan producers, as the ban has become effective right at the start of the harvest season. We estimate that Moldova faces a drop in export revenues in this sector of about USD 65 m – again assuming that it remains in place for a whole year. Incorporating canned fruits into the calculation, the costs increase to 76 m USD.

While all previous measures are de-facto import bans, Russia has also increased the import tariff rates for some Moldovan products. Based on the 2011 CIS Free trade agreement, Moldova currently could export almost all goods duty-free so far. In July, however, Russian representatives announced a raise in the import tariffs for in total 19 product groups. The tariff rate for the affected goods (mostly agricultural products, food and furniture) is to be increased to the higher „Most Favoured Nation (MFN) Tariff Rate“ which applies to countries without preferential trade agreements. This would suggest a decline in demand for Moldovan products. However, most products affected by the tariff increase have already been banned before. GET Moldova modelled the expected additional decline, which suggests an only moderate decrease in exports of about 7m USD as a result of the tariff increase.

Overview on recent trade restrictions

Product group	Type	Start	Costs/year, (USD m)
Wine and spirits	Import ban	Sept. 2014	45
Meat	Import ban	July 2014	17
Fruits and canned fruits	Import ban	July 2014	76
19 product categories	Increase in tariff rate	July 2014 (announced)	7
		Total costs	145

Source: Own analysis

In total, due to the existing and newly announced measures, we expect a decline in export revenues of around USD 145 m per year. This corresponds to a reduction of exports to Russia of 25% and is equal to about 2% of GDP. This shows clearly that the trade restrictions have a significant impact on the economy. However, the shock is unlikely to be of such a magnitude that it will threaten economic stability.

Conclusions

The remaining question is what Moldova can do to mitigate the shock. Important instruments are the official dispute resolution mechanisms of the WTO and of the Economic Council of the CIS. Similarly, the EU has initiated a WTO conflict settlement for the Russian import ban on EU pork meat. The EU argues in front of the WTO that the Russian measures are arbitrary, disproportional and not based on scientific facts.

In addition to dispute settlement mechanisms, the Moldovan government should offer targeted support for the sectors and companies most affected. GET Moldova has made recommendations directed at reducing the negative impact of which several have been implemented already. To be clear, retaliating with trade bans on Russian goods (e.g. beer) imported to Moldova, is counter effective and should not be part of the government's policy response. Indeed, this would only result in even higher costs for Moldovan consumers due to an increase in prices and a smaller variety. Also, being a member of the WTO and a reliable international partner, Moldova should act WTO-compliant, irrespective of Russian measures.

The main focus should be instead on improving access to new markets within or outside the EU. Export promotion should play a large role in this context. Indeed, the experience from the 2006 wine embargo shows that, in the medium - and long-term, the Moldovan economy can evolve more competitive from such a trade embargo

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The German Economic Team Moldova (GET Moldova) maintains a dialogue on economic policy with decision-makers of the Moldovan government since 2010.
It is funded by the Federal Ministry of Economic Affairs and Energy (BMWi) within the framework of the successor of the TRANSFORM programme of the German government

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