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Raising Soviet Food Import Costs: Can The West Do It?

Soviet grain imports have grown enormously over the past decade and this year will account for one-fifth of all grain bought in international markets. Three consecutive harvest failures have made Moscow's need for foreign grain especially pressing. Five major exporters--the United States, Canada, Australia, Argentina, and the EC--account for some 90 percent of world grain exports and a similar portion of the 45 million tons we expect the USSR to import during the year ending in June. ~~(C NF)~~

The USSR's dependence on a few Western countries for an important share of its food needs--one fifth of Soviet grain requirements will be imported this year--suggests an opportunity for the West to exploit. A unilateral price increase by the United States would encourage other exporters to raise prices to the Soviets. Other forms of market action, such as an embargo or cartel, designed to deny grain to the USSR or raise Moscow's food import costs seem unlikely to succeed. Success depends on active exporter cooperation, an ingredient now almost entirely lacking. ~~(C NF)~~

Embargo

Should the major grain exporters act together, the threat of an embargo on grain shipped to the USSR is awesome in light of the magnitude of Soviet import dependence. Without Western grain the Soviet livestock program would likely collapse. The meager gains in food supplies made in the last decade would be reversed. ~~(C)~~

During the 1980 embargo, however, exporter unity was largely absent. Most major non-US grain exporters gave lip service in support of the embargo but conducted business as usual. As a consequence, Moscow was able to replace half of the denied US grain through direct purchases from major non-US exporters. Even with exporter compliance Moscow could have continued grain deliveries by resorting to transshipments, swapping contracts, falsifying destinations, or arranging reexport--actions difficult to monitor. ~~(C NF)~~

Cartel

Proposals that major exporters establish a grain cartel similar to OPEC have surfaced periodically. An effective cartel could, of course, be used to add to exporter revenues by charging higher prices across the board or to discriminate against a single consumer, such as the USSR, by denying grain or charging higher prices for that customer alone. ~~(C)~~

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The obstacles to a cartel are overwhelming. Non-US exporters would almost certainly be reluctant to sweep aside the market structure that has facilitated a doubling of world grain trade during the last decade, bringing them enormous benefit. Specifically, they would doubt the ability of the United States to drastically recast its marketing system, question US willingness to absorb the majority of cartel costs (as Saudi Arabia does for OPEC), fear that a change of administrations could lead to a US renunciation of the cartel, and resent the loss of control over international sales or domestic production that would be necessary for the cartel to function effectively. ~~(C)~~

Price Action

A destination surcharge or export tax levied on grain shipped to the USSR could, under certain conditions, increase revenues to exporters and inflict higher food costs on Moscow irrespective of Soviet defensive actions. Price discrimination against the Soviet Union offers several advantages over other forms of market action:

- If the USSR did not curtail grain imports, total world sales would not be affected and participating exporters would achieve higher overall revenues. In contrast, an embargo ensures revenue losses because of smaller total sales and lower prices.

- The USSR could try to maintain grain import levels but avoid the surcharge by placing greater reliance on exporters that fail to impose a surcharge and by using market deceptions such as transshipments and diversions enroute to get grain from surcharging countries. Either way, however, the Soviets would still pay above market prices for grain as third countries and traders raise prices toward the surcharge level in order to increase their profits. No matter how much "leakage" occurred, grain costs to the USSR would rise.

- If the USSR cut grain imports in favor of value added products--meat, soybean meal, and the like--the world market price of these commodities would rise, again forcing up the Soviet food bill.

- Should the USSR be forced to reduce its imports of grain and other agricultural products, it would pay a price in terms of the associated economic slowdown, particularly in the livestock program. ~~(C)~~

Any collective action against the USSR involving international markets would require a number of difficult legal and economic adjustments. In all cases, US leadership would be required because of its central role in international grain markets. ~~(C)~~

Legal Adjustments

The USSR is not a GATT signatory and, therefore, lacks the protection that most other countries enjoy in trade matters. However, at least in the United States, discriminatory price action would be more difficult to impose from a legal standpoint than an embargo. The Export Administration Act of 1979 authorizes the President to stop commodity exports under certain situations such as domestic shortage. He is not, however, currently empowered to impose taxes, duties, or other charges on exports. All such measures fall under the taxing authority of Congress, which would have to pass the required legislation. ~~(C)~~

Governments in other major exporting countries generally maintain greater control than the United States over grain exports and prices.

- The Canadian Wheat Board and the Australian Wheat Board maintain direct control over the destination and price of all wheat exports. These boards would have the authority to impose a surcharge on wheat exports destined for the USSR, but discriminatory pricing against a major customer would certainly touch off a political hue and cry by producers. Barley and other coarse grains are presently handled by private firms and state boards.

- Through export rebate certificates, the EC Grain Management Committee decides how much grain will be offered for export and what subsidies will be paid to sell higher cost EC product in the world market. The Committee could increase the price to the Soviets by reducing the amount of the rebate on grain specifically destined for the USSR.

- The Argentine Grain Board plays a minor role in controlling exports and allows private firms to make sales without necessarily disclosing the grain's destination. Thus, some strengthening of the Board's charter would be necessary to effectively institute an export tax. ~~(C NF)~~

Economic Considerations

Any proposal that affects exporters' markets is apt to be viewed with great skepticism. Exporters have enjoyed a ten-fold increase in hard currency sales of agricultural products to the Soviet Union over the last decade. In 1981, Moscow spent a record $12 billion for such imports, about half for grain. The major non-US exporters recognize their growing dependence on the USSR as a market for grain. The share of all wheat and coarse grains exported by Canada, Australia and Argentina to the USSR increased from 8 percent in 1978/79 to 43 percent in 1980/81. In Argentina, where the shift has been most dramatic, roughly 80 percent of both wheat and coarse grain exports were shipped to the USSR last year. Argentine President Galtieri recently stated that he is "mortified" by his country's dependency on the Soviet market but sees little alternative for the disposal of excess grain production. Most non-US exporters have ambitious plans to step up grain production in the coming years, with an eye toward the Soviet market. Last year, for example, France began negotiations with the Soviets for a long term grain agreement (LTA) in hopes of expanding foreign demand for its increased wheat output. ~~(C)~~

Even though exporters would be wary of tampering with the market, a discriminatory price action has, from the major exporters' perspective, a number of advantages over other forms of action. It would be aimed at obtaining higher prices while maintaining total sales, thus lessening the producer pressure that would certainly occur should an attempt to reduce total exports be made. Also, it would not discriminate against both friends and foes alike, as would a cartel. A selective price increase requires less cooperation among exporters to achieve its desired result than an embargo. ~~(C)~~

The effectiveness of a selective price action would depend on a host of interrelated factors:

- Exporter Cooperation: The States undoubtedly would need to take the lead, promising to bear the brunt of exporter costs should total revenues fall below pre-action levels. Moreover, to gain cooperation the United States probably would have to agree to exclude from the surcharge all grain under long-term agreements. These agreements guarantee Moscow about 10 million tons of grain annually at market prices, covering perhaps one-third of future Soviet needs.

- Timing: Unless a surcharge suddenly catches the Soviets unaware and at a time when their own grain production and reserves are low, Moscow will have time to lessen the impact of higher prices. Arranging a sudden move would be extremely difficult. Gaining agreement of other exporters could require lengthy negotiations over the size of the surcharge, market shares, and date for implementation, probably tipping Washington's intention. Conditions in the world grain market would weigh heavily on exporter attitudes, and right now surpluses are the key problem.

Unilateral US Price Action

If the United States decided to unilaterally raise prices of grain exported to the USSR, the move would raise Soviet import costs. Even if the Soviets choose to forgo US grain, other exporters undoubtedly would exploit the opportunity to increase revenues. Argentina, for example, exacted premiums of up to $70 per ton for grain sold to the Soviets during the 1980 embargo. ~~(C)~~

USSR: Impact and Reaction

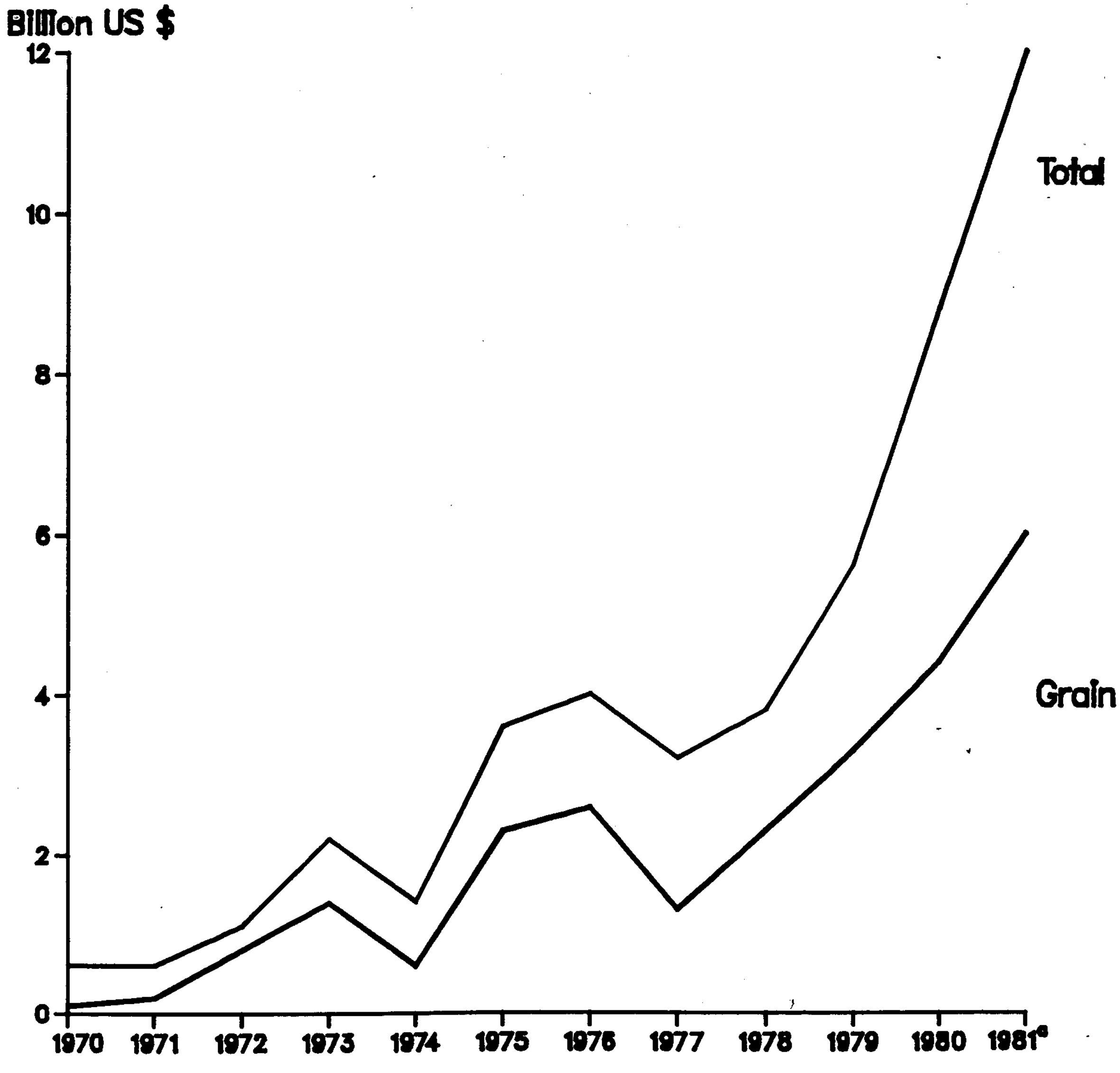
Barring denial actions by exporters, we expect the USSR to import a minimum of 30 million tons annually over the next several years, even if domestic grain production recovers sharply. Should an export tax, say of $100 per ton, be imposed, Moscow's costs would be inflated by at least $2 billion.

The Soviet Union has experienced a sharp erosion in its hard currency position over the past year. This weakening is primarily due to a combination of increased imports from the West--especially grain--and soft Western markets for Soviet crude oil and other primary product exports. The additional costs occasioned by a surcharge would add significantly to the Soviet hard currency problem, but the USSR is still in a fundamentally sound financial position and not on the brink of financial disaster. ~~(C)~~

Moscow's reaction to a surcharge, then, would depend primarily on the size of the domestic grain harvest and the availability of foreign exchange. We believe Moscow would try to adjust to the price increase without a large-scale reduction of livestock inventories and without reducing per capita meat consumption. Increasing meat imports and eliminating growth in livestock inventories, product output, and grain stocks for a year or two might be the initial policy. ~~(C)~~

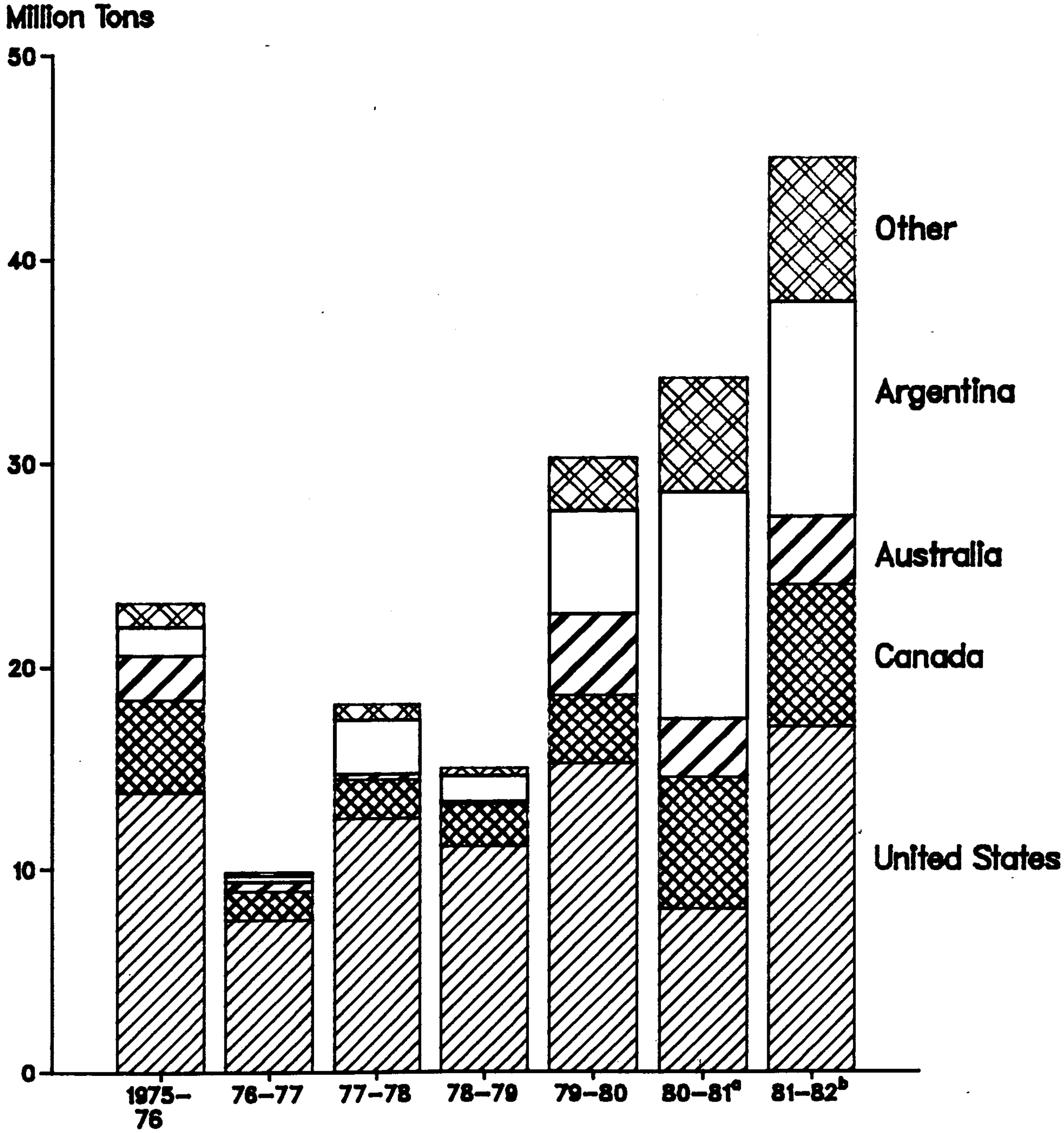
These options carry considerable risk, especially if grain production falls substantially below 220 million tons. Indeed, last year was the third in succession of increasing food shortages, mostly in the area of quality foods--meat and dairy products. Rationing of these items, mostly in the form of informal purchase limits, has become more frequent and widespread since the winter of 1980/81. The mood of consumers is generally one of pessimism and resigned acceptance. Soviet workers are still a long way from venting their dissatisfaction as have Polish workers. ~~(C)~~

USSR: Total Hard Currency Agricultural and Grain Imports



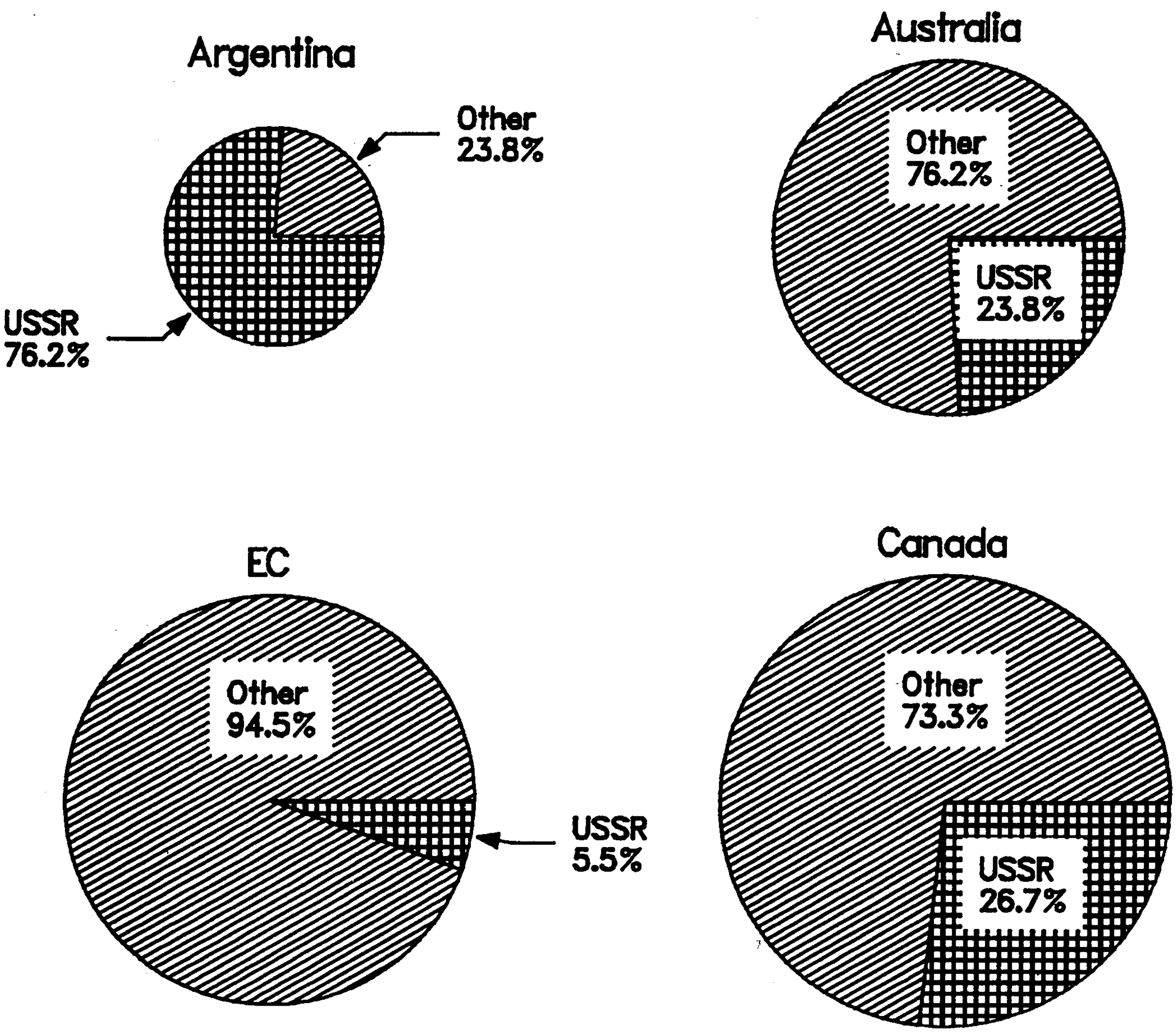
a. Estimated.

USSR: Grain Imports, by Source



a. Preliminary.
b. Estimated.

Major Non-US Wheat Exporters: Soviet Share of Total Exports[a]
July 1980–June 1981



a. Including wheat flour.