

MEMU Supplement No. 08-2005

A Ukrainian Sugar Crisis

In mid-July 2005 wholesale prices for sugar increased by 76% yoy to reach UAH 4.5 per kg, which is three times the world market price. The rapid increase in the wholesale price had an immediate effect on prices at the retail market: Depending on the region and the point of sale they ranged from UAH 4.8 to 5.8 per kg.

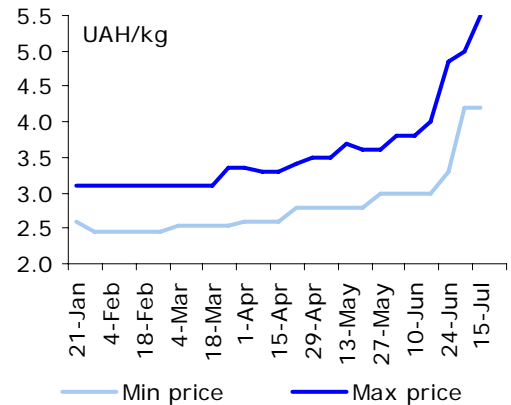
The rise in the sugar price was caused by several factors. During the summer months Ukraine's market traditionally experiences seasonal increases in the demand for sugar, which households use for making preserves. On the other hand, the level of domestic beet sugar production, which proved to be uncompetitive relative to other countries, is not enough to satisfy the domestic demand for sugar. Over the last several years the amount of beet sugar produced in Ukraine never exceeded 1.8 m tons, whereas 2.1 to 2.2 m tons of sugar are consumed annually. In previous years the resulting deficit was covered by domestic refining of raw cane sugar, imported under the privileged within-quota¹ import duty of 5 EUR/ton (as opposed to the over-quota import duty of 300 EUR/ton), as well as by imports of sugar via the Special Economic Zones and some illegal imports. In 2005 the Ukrainian Parliament did not support the opening of a privileged import quota, thus making the 300 EUR/ton import duty effective for all raw sugar imports. This made legally imported raw sugar very costly and, therefore, unattractive. Also, the recent abolition of the Special Economic Zones and the tightening of border and customs controls under the governmental "Stop Smuggling Program", limited largely both legal and illegal imports of white sugar to Ukraine. Taking into account that the demand for sugar is price-inelastic, the reduced sugar supply led to a substantial increase in its price.

Although prices for sugar are expected to drop after the new sugar beet harvest starts, it is very likely that the existing market imbalances will continue to provoke sharp price fluctuations in the future should the state's over-protectionist policies not be changed. At this time the Government is not empowered to open import quota without Parliament's approval. That is why, the sugar industry so strongly lobbies Parliament to delay the opening and limit the volume of Tariff Rate Quotas (TRQs). By delaying and limiting TRQs, Parliament can maximize the monopoly rents that accrue to those who receive TRQs licenses. By limiting TRQs, Parliament can boost the profits of those sugar producing and trading interests who hold back sugar stocks.

To prevent similar situations at the sugar market in 2006 and later, the German Advisory Group and IER worked out the following recommendations. Firstly, the state policy should aim at preventing deficits at the sugar market. Whenever the domestic price for sugar exceeds a certain previously defined level, the Cabinet of Ministers should be empowered to immediately open an additional Tariff Rate Quota without interference from Parliament or other authorities. Secondly, all import licenses under the Tariff Rate Quotas should be publicly and transparently auctioned by the Government and given to the highest bidder. This will ensure that the state will control the TRQ rents. Lastly, the amount of TRQs to be auctioned in any marketing year should be determined right after the volume of the domestic sugar production for that year is known but generally no later than by December.

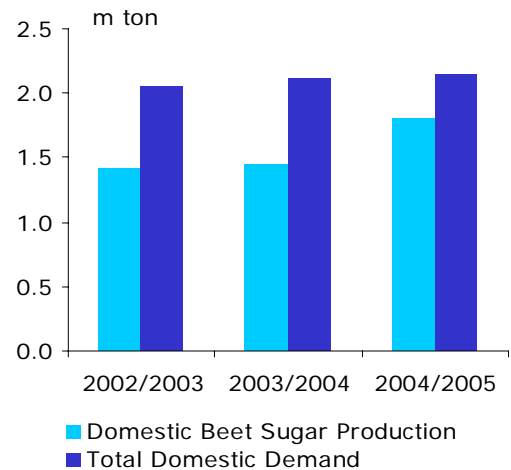
The proposed measures will make the sugar market more flexible and, thus, less prone to supply shocks. They are also likely to encourage the domestic sugar industry to increase its efficiency and competitiveness.

Development of Retail Prices on Sugar in 2005



Source: APK-Inform

Sugar Balance



Source: APK-Inform

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¹ Within-quota and over-quota import duties relate to the Tariff Rate Quota (TRQ) trade tool.


Quarterly Trends

National accounts **		Q4 02	Q1 03	Q2 03	Q3 03	Q4 03	Q1 04	Q2 04	Q3 04	Q4 04	Q1 05
GDP	UAH bn	63.3	51.5	60.0	75.6	77.1	64.7	79.0	100.5	100.6	82.5
GDP (real)	% yoy	6.1	8.4	10.0	6.8	12.1	12.7	13.7	14.0	8.5	5.0
Households consumption (real)	% yoy	11.2	10.2	14.4	11.2	13.6	14.6	16.8	13.1	16.2	16.4
State consumption (real)	% yoy	2.9	15.0	17.8	19.2	9.0	3.3	1.0	5.0	10.1	5.2
Gross fixed capital formation (real)	% yoy	5.7	9.0	20.4	24.3	9.0	18.4	6.5	4.6	12.9	-2.6
Exports of goods and services (real)	% yoy	17.0	9.9	9.8	9.8	11.6	18.1	19.9	10.5	8.6	0.1
Imports of goods and services (real)	% yoy	6.7	13.8	16.2	17.4	17.7	13.8	7.3	6.7	7.8	6.6
Agriculture, hunting, forestry (real)*	% yoy	1.3	4.0	-13.7	-22.5	6.7	-4.4	0.9	35.7	9.9	5.9
Manufacturing industry (real)*	% yoy	11.5	12.0	15.4	23.0	20.1	23.9	16.3	12.5	9.4	7.8
Construction (real)*	% yoy	2.7	18.2	24.8	30.9	16.9	29.9	30.6	16.4	3.9	-5.9
Trade, repair services (real)*	% yoy	3.5	7.2	15.1	22.6	29.6	23.6	35.0	2.7	13.7	-1.5
Transport (real)*	% yoy	11.0	10.0	11.5	15.9	11.7	10.1	8.0	12.3	10.5	7.3
Balance of payments											
Current account balance	USD bn	1.0	1.1	0.7	0.7	0.4	1.6	2.3	1.7	1.2	1.7
Current account balance	% of GDP	7.9	11.2	7.0	5.0	3.0	13.5	15.5	8.8	6.2	10.8
Trade balance in goods	USD m	225	309	-42	-155	-381	933	1552	774	482	1051
Trade balance in services	USD m	382	387	399	362	409	332	153	377	270	257
Current transfers	USD m	520	500	526	574	584	475	758	720	623	624
Direct investment (FDI)	USD m	300	238	454	390	329	334	614	422	345	231
Portfolio investments	USD m	-520	-825	640	-444	-293	60	-406	781	-511	-114
Gross international reserves	USD bn	4.4	4.6	6.2	6.7	6.9	7.9	9.6	12.1	9.5	13.1
Fiscal indicators											
Consolidated fiscal revenues	% of GDP	28.1	31.6	31.7	30.1	28.6	27.2	26.9	26.3	25.9	32.1
Personal income tax	% of GDP	4.9	5.7	5.7	5.3	5.1	4.4	4.1	3.8	3.8	4.3
Enterprise profits tax	% of GDP	4.3	5.7	5.1	4.8	5.0	3.9	4.0	4.1	6.1	4.8
Value-added tax	% of GDP	6.1	6.2	6.3	5.8	4.8	6.2	5.7	5.1	4.1	8.6
Excise tax	% of GDP	1.9	2.1	2.2	2.1	2.0	2.1	2.1	2.0	1.8	2.0
Consolidated fiscal expenditures	% of GDP	27.3	27.7	29.2	27.9	28.8	25.3	26.5	26.8	35.2	28.3
Current expenditures	% of GDP	na	na	26.3	24.2	24.3	22.4	22.7	21.7	27.2	26.5
Capital expenditures	% of GDP	na	na	3.0	3.7	4.4	2.9	3.8	5.1	8.0	1.8
Consolidated fiscal balance	% of GDP	0.7	3.8	2.5	2.2	-0.2	1.9	0.4	-0.5	-9.3	3.7
Privatisation receipts	% of GDP	0.3	0.6	1.0	1.0	0.8	1.5	3.7	3.5	1.0	0.2
Labour market											
Average wage (real)	% yoy	17.7	12.3	19.1	19.9	14.9	19.9	18.6	14.7	15.4	15.0
Household income (real)	% yoy	65.6	-1.2	8.6	10.0	8.7	11.7	16.3	11.3	16.6	24.0
Unemployment rate (ILO methodology)	%	11.1	9.4	8.8	9.2	9.0	9.3	8.3	8.1	8.7	-
Banking system											
Monetary aggregate M0	% yoy cum	35.8	32.4	37.0	30.5	25.3	29.1	25.6	37.1	27.9	28.2
Monetary aggregate M2	% yoy cum	42.2	47.8	54.6	49.9	47.6	45.4	44.8	51.5	32.3	38.9
Household deposits in national currency	% yoy cum	72.5	73.4	74.7	65.0	66.1	69.4	67.3	67.9	26.2	28.3
Household deposits in foreign currency	% yoy cum	59.3	71.2	70.2	70.4	77.5	67.0	61.7	55.2	54.3	51.8
Com. bank credits in national currency	% yoy cum	54.4	63.7	71.2	73.0	61.7	56.8	52.1	44.3	29.4	28.3
Com. bank credits in foreign currency	% yoy cum	40.3	44.1	48.4	57.7	60.9	63.6	56.2	43.5	32.2	33.1
Long-term com. bank credits	% yoy cum	92.5	110.6	156.4	164.0	157.9	141.7	102.7	82.7	57.1	49.5
Long-term com. bank credits	% of total	28.2	31.3	37.4	40.1	45.0	47.4	49.3	50.9	54.2	54.4
Average lending rate on national cur. credits	% p.a.	21.8	18.0	17.2	17.2	17.7	17.2	16.6	17.0	17.6	17.0
Average lending rate on foreign cur. credits	% p.a.	11.3	12.5	12.6	11.7	10.9	12.2	12.1	12.6	12.2	12.1

SOURCES: National Bank of Ukraine, State Committee of Statistics, State Treasury, Ministry of Finance, IER estimates

* change in value added

** preliminary

Notes:
yoy year on year change

p.a. per annum