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CEI GLOBAL REPORT

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Russia-Ukraine war and trade sanctions

The war between Russia and Ukraine will surely have significant and varied consequences on the economic, commercial and financial activity of both countries as well as of the rest of the world.

One of the most noticeable economic and trade impacts is the effect on exports and prices: the importance of the countries in conflict as producers of some primary goods has been directly reflected in the rise in prices of these commodities. The most relevant case is probably wheat. Russia and Ukraine are responsible for almost a third of world exports of this grain. However, the increases are not limited to this cereal, but also to corn, sunflower oil, fertilisers, aluminium and nickel, among others. Those countries whose food security depends on imports from the conflict zone will have to face price increases and will possibly need to find new suppliers (see Africa).

On the other hand, the response of most Western countries has focused on economic sanctions against Russia, which will likely end up having repercussions not only on the target but also on the global economy.

Sanctions against Russia

The measures applied since the Russian invasion of Ukraine starting on 24 February have been growing in strength and scope. They began with the extension of the lists of people and companies restricted from carrying out financial transactions and of those who suffered financial asset freezes. Subsequently, restrictions were applied to the exports of goods and services that may have military use, the freezing of Russian Central Bank reserves held abroad, and the disconnection of certain Russian banks from the SWIFT financial communications system which allows the transfer of funds between financial institutions and payments for foreign trade and debt securities. A changing feature is the degree of coordination that existed between several countries to adopt these sanctions: the United States, European countries –including Switzerland–, Canada and Japan.

It should be noted that these sanctions are an extension and deepening of other measures taken since 2014, mainly by the United States and the European Union, such as the blocking of assets of certain government officials and their companies and the ban on trade relations with some Russian companies connected to the annexation of Crimea by the Russian Federation.

One of the possible consequences of the sanctions is a sharp reduction in gas sales from Russia to Europe, which would not be in a position to meet that lower supply, according to a JPMorgan report. Replacing gas of Russian origin is complicated as there are no connections between terminals that receive liquefied natural gas (LNG) –a substitute for natural gas– and the gas distribution network, and there is a shortage of LNG regasification plants. The only possible option in the short term seems to be rationing demand.

The Russian economy will also suffer the consequences: there will be less production, lower energy exports, which adds to the financial, economic and commercial isolation of greater or lesser degree. There would be a risk of bank-runs regarding foreign currency deposits and a possible freeze of accounts. Large consulting companies forecast a drop in GDP of 7% (JPMorgan, Goldman Sachs) and 9% (Bloomberg).

Effectiveness of economic sanctions

The effectiveness of such measures has been questioned. As an example, the impact of the measures implemented since January 2014 against Russia was estimated to be less than the consequences of the fall in the price of oil in 2014 and the COVID-19 pandemic during 2020. A possible explanation is that they affected specific companies and people more than the Russian economy, both at the general and sectoral level.

If trade embargoes reached an entire sector rather than certain companies, the impact would be greater. According to a simulation made by the Kiel Institute for the World Economy, if the United States, Europe, Japan, Canada, Australia and New Zealand stopped trading gas with Russia, Russian GDP would fall 2.9%; if the embargo were on oil, the fall would be 1.2%. In contrast, EU's GDP would hardly change.

EUROPE

Energy price surge

In 2021, the European Union recorded the highest inflation in the last 25 years, mainly driven by the increase in energy prices (see CEI Global Report, February 2022). In this context, the countries of the bloc must now face the economic consequences of the military invasion of the Russian Federation to Ukraine and the economic retaliation sanctions.

The main concern of the EU officials is gas costs (which reached record values after the invasion), because nearly 40% of the natural gas imported by the European continent comes from Russia. Germany decided to suspend the final approval of the Nord Stream 2 gas pipeline, and the possible suspension of the shipments would worsen an already complicated situation.

The price increase is also seen in other fuels exported by Russia such as oil (which exceeded the barrier of 100 dollars per barrel), and coal. This situation is expected to have serious effects on the European inflation this year. Before the war, many analysts forecast that this year's overall price increase would be lower than in 2021 because it would have overcome some problems which resulted in energy increases last year (see CEI Global Report, November 2021), but this is now called into question.

EU investment in microchip production

The European Commission presented the European Chips Act, a legal tool with which the authorities of the bloc intend to achieve a fourfold increase in the production of semiconductors in the EU countries. The regulation is aimed at progressively increasing the microchip production capacity to cover 20% of the global demand by 2030.

The European initiative responds to the provision problems that took place in the past, resulting from the exponential increase in the demand of integrated circuits that was not accompanied by the corresponding growth of supply, and that forced the suspension of production lines in different industries. With this, legislators seek to reduce the European dependence on third-country semiconductors, mainly from Asia.

The European authorities plan to add 11.0 billion euros in investments (public and private) for research and development to the 30.0 billion euros that are already included in the European budgets and recovery funds. The plan also includes the construction of factories that will boost large-scale production, and the creation of alliances with other countries to create supply chains and avoid the bottlenecks that have arisen in recent times.

EU ruling against Poland and Hungary

The Court of Justice of the European Union (CJEU) rejected the demands made by Poland and Hungary, which sought the annulment of the European mechanism that conditions the access to the EU funds to the respect of the rule of law principles. The regulation of the bloc allows the European Council to suspend the transfer of funds to the member states in case they fail to comply with the mentioned principles, which was objected by the Hungarian and Polish authorities.

The Court endorsed the position of the European Council, Commission and Parliament, which were supported by Germany, Belgium, Denmark, Spain, Finland, France, Ireland, Luxembourg, the Netherlands and Sweden; this is a heavy setback for Hungary and Poland, which face manifold accusations of rule of law breaches (see CEI Global Report, December 2020) and whose access to the structural, agricultural and recovery European funds could be suspended.

SOUTH AND CENTRAL AMERICA

Venezuela might resume the sales of oil to the United States

The President of Venezuela, Nicolás Maduro, welcomed in the Miraflores Palace, seat of the government, a team of US officials who travelled to Caracas with the intention of holding talks, among other things, about the possibility that the US can lift the embargo on Venezuelan oil.

Venezuela's main export product has not been allowed to be traded in the American market since 2019, when Donald Trump imposed sanctions to the Maduro government. Nevertheless, this situation can change due to Joe Biden's decision to ban the imports of oil, natural gas and coal from Russia, as a response to the invasion to Ukraine. Consequently, oil imports from Russia could be replaced by the Venezuelan crude oil.

Insufficient growth for the recovery from the pandemic

According to the Social Panorama of Latin America published by ECLAC, the economic growth experienced by the region in 2021 (which was estimated at 6.2% by the organisation) was not sufficient to reverse the damages caused by the COVID-19 pandemic in social and labour matters.

According to the report, in 2021, the region registered unemployment rates and levels of poverty and extreme poverty higher than those recorded before the pandemic. Last year, extreme poverty might have reached 13.8%, meaning that the number of people in this situation is likely to have increased from 81 million (2020) to 86 million.

ECLAC suggests that, in order to reinforce the recovery in the short term, the countries in the region will have to keep the emergency social protection measures that they implemented in 2020, in addition to continuing with the proper health policies. The body recorded a remarkable reduction in public expenditures aimed at reversing the social disruption caused by the pandemic. While the emergency transfers announced by the countries in the region went up to US$ 89.7 billion in the first ten months of 2020, in the same period of 2021 they were only US$ 45.3 billion.

CAF places bonds for the reactivation of the region

The Development Bank of Latin America (CAF) announced the placement of a 5-year-bond for US$ 650 million and a 2.25% interest rate to support, with the funds raised, the economic and social reactivation of Latin America and the Caribbean.

The bonds were acquired mainly by fund management services, central banks, commercial banks and public institutions, and the operation was in charge of BNP Paribas, Goldman Sachs International, Morgan Stanley and Nomura.

The international organisation informed that the resources obtained after the emission "come from international markets at competitive rates, and help foster sustainable development of the region by financing strategic projects, providing technical cooperation and knowledge products".

NORTH AMERICA

US and Japan agree on the elimination of tariffs on steel

The United States and Japan announced the elimination of the Trump era tariffs on the imports of Japanese steel. The agreement will take effect on 1 April and establishes a tariff-rate quota of 1.25 million metric tonnes of steel (amounting to the average of Japanese steel imported to the US in 2018 and 2019) that will be able to enter annually to the North American country without having to face the additional tariff of 25% set in 2018.

The agreement, like that reached in October last year with the EU (see CEI Global Report, November 2021), demands that the steel imported from Japan is fully manufactured in said country so as to benefit from the tariff exemption and it includes several measures to approach the excess in manufacturing capacity at global level. On the other hand, it is worth emphasising that –contrary to what was agreed on with the European bloc– the agreement does not contemplate the elimination of the 10% additional tariffs on the imports of Japanese aluminium.

The Minister of Economy, Trade and Industry of Japan, Hagiuda Koichi, declared that, although the measures adopted by the US are positive, Japan will continue to strongly urge said country to resolve this issue completely in such a manner that it adjusts to the WTO standards.

USMCA: ruling in favour of Canada in dispute over safeguard on solar panels

On 15 February, the dispute settlement panel of the United States-Mexico-Canada Agreement (USMCA) that analysed the disagreement over the application of the safeguard by the United States on photovoltaic products of crystalline silicon imported from Canada ruled in favour of the latter country.

Canada held consultations for the first time regarding the measure when this was imposed by the Trump administration in 2018, within the framework of the North American Free Trade Agreement (NAFTA). Later, it reiterated its claim in the sphere of the USMCA and, last June, it requested a panel after no solution had been found in the phase of consultations (see CEI Global Report, July 2021).

The final report of the panel confirmed that the safeguard adopted by the US is unjustified and represents a violation to the USMCA. According to the ruling, the imports coming from Canada did not constitute a "substantial share" of the total of the American imports and they could not "have contributed importantly" to any serious economic damage allegedly suffered by producers.

The US government has 45 days –after the final determination of the panel– to exclude the Canadian imports from the safeguard measure. Upon failure of doing so, Canada will have the possibility of adopting trade retaliations.

It is worth emphasising that, prior to the ruling, President Biden had issued a proclamation to renew the safeguard measure for another four years. At the same time, it instructs the United States Trade

Representative to start negotiations with Canada and Mexico regarding an agreement that could lead to the suspension of the measure on imports from both countries.

Discrepancies between the US and Mexico regarding illegal fishing

The Office of the United States Trade Representative (USTR) presented, at the beginning of February, a request for consultations regarding the implementation of measures for the protection of the vaquita, the prevention of the illegal fishing and traffic of totoaba, under the scope of chapter 24 of the USMCA.

According to the statement, the US seeks to ensure that Mexico meets its environmental commitments within the trade agreement. The vaquita is the smallest cetacean in the world and it is critically endangered. The incidental bycatch by banned gillnets, mainly those used to catch shrimps and totoaba fish, in the Northern Gulf of California, are the main cause of mortality of this type of porpoise.

Although the trade of totoaba (also known as white sea bass) is prohibited by the Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES), it is highly demanded because its swim bladder is considered to be a source of medicinal properties by some Asian cultures.

It is the first time that a government invokes the environmental provisions of the USMCA. According to the agreement, if the parties do not succeed in solving the conflict within the 30 days following the reception of the request, a meeting of the Commission on Good Practices, Conciliation and Mediation can be summoned. In case no solution is found, a panel can later be called in order to decide on the trade sanctions.

On the other hand, since 7 February, Mexican fishing boats have been banned from accessing the ports of the United States in the Gulf of Mexico, due to the increase in the illegal fishing of red snapper or huachinango in waters of the US territory. This prohibition derives from a report by the National Oceanic and Atmospheric Administration (NOAA) through which a “negative certification” is granted to Mexico due to its illegal fishing in American waters and the incidental bycatch of sea turtles.

In April 2021 a similar conflict had arisen, when inspectors of the United States found Mexican shrimp fisher boats that did not use devices to prevent the turtles from getting trapped in the nets. This made the Mexican shrimp lose the certification to be sold in the neighbouring country and the Mexican government had to spend almost 6 months to reverse the American sanctions.

State company to exploit lithium in Mexico

The president of Mexico, Andrés Manuel Lopez Obrador, announced the creation of a state company to exploit lithium in Mexican territory, and described the mineral as a strategic natural resource for the country.

Although it is well known that there are reserves of this mineral in Mexican territory, their magnitude is still under discussion. Mexican former Secretary of Economy Graciela Márquez denied in 2020 that the state of Sonora hosts the largest deposit in the world, as had been expressed after estimations of a study made in 2018.

At present, the deposits in the country are still in their exploratory phase and the biggest is in the hands of a company whose majority shareholders are of Chinese origin. In that respect, the Mexican President was critical of the concession granted and expressed: “When those concessions were awarded, it was not for lithium, it was for mineral exploitation; lithium is something different, it belongs to the Nation, not like gold or silver or copper”. And he added: “Besides, we do not want to be a territory of conflict between powers. Neither Russia, nor China, nor the United States”.

ASIA AND OCEANIA

China introduces document on food security

Food security remains one of the priorities for China. This year, the concern over this issue was included in the "No. 1 Central Document", considered an indicator of high-priority political topics for the Chinese government.

The document announces that measures will be taken to ensure that the areas sowed with cereal remain stable and that the production is still above 650 million tonnes. Besides, it is mentioned that efforts will be made to strengthen the production capacity of soybean and other oilseeds, and that the supply of key products like pork and vegetables will be guaranteed.

With respect to the increase in the production of soybean and maize, the Minister of Agriculture and Rural Affairs, Tang Renjian, said that the authorities will improve the subsidies for producers, and encourage those producers from the northeast of China –main production area– to plant more soybean and promote the soybean and corn intercropping technology, guaranteeing a stable production.

According to the 14th Five-Year Plan (2021-2025), prepared by the Ministry of Agriculture and Rural Affairs, it is expected that China reaches an output of 23 million tonnes of soybean. The Asian country is the greatest importer and consumer of soybean in the world. In 2021, it imported more than 90 million tonnes, and in 2020 it surpassed 100 million tonnes. The United States, Brazil and Argentina are the main suppliers of soybean. With a self-sufficiency rate of less than 20%, soybean is one of the crops for which China mostly depends on imports.

China to adopt measures to stabilise the industrial sector

According to China's State Council, the recovery of the country's industrial sector is not solid, a reason why measures will be taken to promote the activity, in special, of the small companies. The Chinese economy faces manifold pressures due to the reduction of demand, the weakness of the real estate sector, and the strict controls amid the COVID-19 pandemic, which affect consumers' confidence and expenditures.

The new measures will include fiscal exemptions and medium- and long-term loans for small companies. Likewise, the Chinese government committed itself to continuing working to stabilise the price of key raw materials and their supply.

India and United Arab Emirates reach trade agreement

On 18 February, India and United Arab Emirates signed a Comprehensive Economic Partnership Agreement (CEPA) during the virtual summit between the Indian Prime Minister, Shri Narendra Modi, and Mohamed bin Zayed To the Nahyan, Crown Prince of Abu Dhabi. The negotiations regarding the agreement were completed in record time, since they had started in September 2021. In addition, both nations set a road map for the future expansion of the mutual cooperation, and issued a joint vision statement called "Advancing the India and UAE Comprehensive Strategic Partnership: New frontiers, new milestone".

In a press release, both leaders expressed their deep satisfaction regarding the continuous growth of bilateral relationships in all sectors, and they expect that by means of this mechanism, a rise from the current US$ 60 billion to US$ 100 billion in bilateral trade takes place in the next five years.

The agreement includes the immediate tariff reduction on 80% of the goods, and the trade approach promotes greater investment in sectors like hotel services, health care logistics, construction and professional services, and promotes cooperation in agriculture, food security, advanced technology, and renewable energies. Besides, it will provide a platform for all the small- and medium-sized companies to participate, collaborate and expand into new markets.

CPTPP: Great Britain to move into the following stage of accession

The country members of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) decided that Great Britain continues the accession process. In a statement, Japan, that heads the UK's Accession Working Group, confirmed on 18 February that said country could proceed to the next phase of market access negotiations to join the Agreement. It is expected that, in the next 30 days, the United Kingdom introduces to the members its market access offer, for instance, in tariff matters. On the other hand, the British Parliament constituted an examining committee to evaluate the accession negotiations, the environmental issues and the impact of the agreement on the people and companies of the United Kingdom.

In November 2017, the Ministers of Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore and Vietnam announced the core elements of the CPTPP, which incorporated an important part of the provisions of the Trans-Pacific Partnership (TPP), from which the United States withdrew during the Trump administration. On 23 January 2018, the 11 CPTPP member countries reached an agreement in Tokyo, Japan, and later undersigned the agreement on 8 March 2018 in Santiago, Chile.

AFRICA

Consequences of the armed conflict for Africa

The military invasion of Russia into Ukraine warned the African countries on the fact that they depend on the imports of basic food products from the countries under conflict. These two countries' share in the imports of wheat from Egypt goes up to 85%, while 65% of the wheat imported by Sudan comes from Russia. Other large countries in the region like Kenya or Nigeria also depend to a great extent on the cereal coming from the countries at war.

The increase in the prices of wheat that had been taking place intensified as a result of the armed conflict. Russian and Ukrainian exports of wheat reached altogether almost 30% of the global exports of said cereal. The sanctions against Russia and the loss of Ukrainian production capacity gave rise to a fall in the cereal supply. Other agricultural products like maize and sunflower oil that Africa imports from both countries might show the same behaviour, likely representing a new threat to food security in Africa that would make it substitute suppliers.

To the food problem, the energy issue must be added, since even though some gas and oil-exporting countries, like Algeria, Nigeria or Angola, can be benefited from the higher prices, for most of them this would imply higher transport costs and a rise in inflation.

The EU to invest 150 billion euros in Africa

The President of the European Commission, Ursula von der Leyen, informed that the European Union will invest 150 billion euros in infrastructure in the African continent, within the framework of the

“Global Gateway” Package, EU’s global investment strategy, after meeting in Dakar with the Chief of State of Senegal and current President of the African Union, Macky Sall.

The plan sets out to contribute up to 300 billion euros in infrastructure in Latin America, Africa and Southeast Asia and can be considered a response to the Chinese initiative “Belt and Road”, also known as the “New Silk Road”, adopted in 2013 by the Chinese President, Xi Jinping.

African Development Bank invests in health infrastructure

The Board of Directors of the African Development Bank Group (AfDB) approved its “Strategy for Quality Health Infrastructure in Africa 2022-2030”, in which it defines its role in addressing the deficits in health infrastructure in the continent.

The strategy focuses on three cross-cutting subjects: the improvement of the internet and communications technology connectivity to strengthen the health information systems and to support innovation; the promotion of regional cooperation and harmonisation of health policies and regulations; and the dialogue over policies and technical assistance.

The COVID-19 pandemic exposed the deficiencies in the national health systems in Africa and it is expected that in the future, the growing population in Africa will place further strain on the healthcare infrastructure. The health facilities are unevenly distributed, with important gaps in rural areas. Only half of the primary health care facilities in Sub-Saharan Africa have access to clean water and adequate sanitation and only one third have access to reliable electricity.

In this context, it is estimated that the health system in Africa needs around US$ 26 billion in capital investments per year. As part of its health agenda, the African Development Bank committed itself to investing US$ 3 billion in the pharmaceutical industry of Africa over 10 years.

CEI GLOBAL REPORT

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Argentina