POLITICAL RISK INVESTING IN EMERGING MARKETS VERSUS ECONOMIC REALITY

Abstract:
Investment risk is always accompanied with “return”, it is one of the most important aspects to evaluate when doing business by private firms or making new decision on overseas investments by governments. According to the report “World Investment and political Risk” provided by the Multilateral Investment Guarantee Agency, investors keep ranking political risk as a prime obstacle for investments into developing markets (Multilateral Investment Guarantee Agency, 2014). The term “emerging markets” originally brought into fashion in the 1980’s by the World Bank economist Antoine van Agtmael. Emerging markets are the world’s fastest growing economies, contributing to a great deal of the world’s explosive growth of trade. By 2020, the five biggest emerging markets’ share of world output will double to 16.1 percent from 7.8 percent in 1992 (Marr & Reynard, 2010). Since the year 2000 share of emerging economies in global GDP (in Purchasing Power Parity) has increased from 37 percent to 50 percent in 2013 (Boumphrey & Bevis, 2013). They are critical participants in the world’s major political, economic, and social affairs and are seeking a larger voice in international politics and a bigger slice of the global economic pie. Recently some events such as Arab Spring, a conflict between Russia and Ukraine, and protests in Brazil against corn upt spending when organizing the World Football championship have increased political risk in those markets. As a result, the issues of political risk analyzed in this article are currently relevant. The aim of the article is to research political risk and its influence on business investments in emerging markets as well as the methods to evaluate such risk precisely as much as possible. This article begins with the introduction to theories relevant for the analysis of the topic. It also presents the political risk and its influences on operations in a emerging market. Then the case study is presented with food industry is chosen for analysis and with application to Russian-Lithuanian situation after Russia has put the sanctions on import of food products (vegetables, meat, fish, milk and dairy products) from the EU member states, Australia, the US, Canada and Norway for a year.

Keywords:
political risk, emerging markets, investment decisions, food industry

JEL Classification: E22, F14, F59
1. Introduction

Political risk is traditionally counted as non-manageable, speculative, and as a fact is mostly only formally integrated into Enterprise risk management, describing it in one or another manner in company’s Risk Policy or Risk management programme. Obviously, political risk can not be eliminated, but it can be managed, especially taking into account spreading experience and using techniques of enterprise risk management system. Political risk together with financial and transactional risks constitutes the international business risk. Foreign exchange rate risk, interest rate and liquidity risk, credit risk and other belong to financial risk (Rugman, 2009, p. 741). Transactional risk arises from factors related to operations provided, they do not come from financial or political risk. For instance, disruptions in business processes caused by disagreements with local partners or inability to effectively manage daily operations because the infrastructure in foreign market is not yet developed enough (Rugman, 2009, pp. 741-742).

The aim of this article is to investigate political risk with application to concrete case – food industry and in relations between emerging markets – Lithuania and Russia. The selection is based on the following reasons. This industry are often escalated on news as the most affected by cold disputes between Russian and Lithuanian politicians. It also sector account for a significant percent of Lithuanian GDP. As to The European Bank of Reconstruction and Development, the export data indicates that the most affected country will likely be Lithuania, where food exports to Russia amount to 2.7 per cent of GDP. The vegetables/fruits export sector appears particularly vulnerable as three quarters of these exports are shipped to Russia. The overall GDP effect appears to be less potent in other sanctioned economies where shares of food export to Russia are less than half a percentage point of GDP (EBRD, 2014). Moreover, the organization Enterprise Lithuania presents that Russia was a major market for Lithuanian food products in 2010; in particular around 30 percent was exported to Russia (Enterprise Lithuania, 2011). Lithuania is believed to be the most vulnerable country targeted by Russia’s agricultural embargo as its exports of the now-banned foods to Russia make up about 2.5 percent of the nation’s GDP, according to BBC (Rianovosti, 2014).


2. Political risk

According to E.P. Hibber (1997), influence of political risk on foreign investments is long lasting, which makes it necessary to evaluate political risk with scrutiny in order to avoid long term damage for the business. Political risk investing in foreign markets is caused by host governments - their decisions and actions (Hibber, 1997). To add, the level of uncertainty in relation to decisions of governmental institutions is indicated by political risk (Rugman, 2009). Stability of position of government is important, for instance, even a stable socialist authority could be more favorable for businesses than a capitalist government with tendency to radical changes in policies (Rugman, 2009).

Furthermore, the source of political risk is not solely the foreign market. According to Rugman, domestic government could also take actions addressed to some country and negatively affect enterprises which have business interests in that country. International environment - international organizations and international events - could also impact the level of political risk faced by international businesses (Rugman, 2009). To continue, political risk could be divided into two broad categories: micro risk or macro risk (Wild, Wild, & Jerry, 2008). On one hand, if the market in general is influenced by political uncertainty, then we should refer to macro risk. In this case all the enterprises in a country are subject to risk. On the other hand, micro risk affects companies which operate a particular industry (Wild, Wild, & Jerry, 2008). In addition, there is a more specific division of political risk too. Country level political risk is generated by tensed, adverse communication between authorities of two countries (Rugman, 2009). In this case if a company is from one of opposing states, doing business in another one may become really complicated.

In addition, there is also a risk of expropriation (takeover of foreign assets invested in a state (Peng, 2007)) which has an impact of lost sales as well as assets and future profits (Wall & Bronwen, 2004, pp. 136-137). Moreover, if a law on obligatory labor benefits is passed, the operating costs in a host market are subject to increase (Wall & Bronwen, 2004). In addition, due to campaigns against foreign goods, overseas capital enterprises may be exposed to a loss of sales as well as growing expenses for public relations to improve public image (Wall & Bronwen, 2004). In the case of civil wars the company as a high risk of losing sales, disturbed production, not only higher costs for security but destruction of property as well (Wall & Bronwen, 2004). Increased taxation also results in lower profits (Wall & Bronwen, 2004). Inconsistent actions of governments are also a source of political risk which increases costs that businesses face. Due to changes in policies business managers cannot forecast future and adapt their strategy effectively (Cavusgil et al., 2002). Political instability is connected to corrupt authorities as well as weak legislative structure (Cavusgil et al., 2002).

Political risk is influenced by the passage of laws, the foibless of leaders, and the rise of popular movements – in short, all the factors that might stabilize or destabilize a
country (Bremmer, 2011, p. 224). Furthermore, personalities in politics are sometimes a significant source of political risk too. It is especially prominent in countries with high concentration of power. For example, under the conditions of current conflict between Russia and Ukraine the international society is actively looking at the actions of Putin and his environment.

Summarizing, there are so many sides of political risk and so many sources of it, that in every concrete situation could be different set of changeable risk factors those strongly influence on identification, assess and management methods of such risk, and these reasons surely bring connected or interested party to interdisciplinary approach, i.e. political science in conjunction with business studies.

3. Main economic features of emerging economies

According to the authors of a book “Doing business in emerging markets”, around the year 2000 some major shifts in economies of developing countries took place. To start with, risks of doing business in developing countries have become more manageable. Also, instead of being simply technologically as well as economically behind emerging markets have experienced larger growth of income in comparison to developed economies, they also have become more competitive technologically. In addition, consumers in emerging markets have increasing purchasing power, which offers more opportunities for businesses. Furthermore, emerging markets are large markets which offer low-cost, in some countries even abundant resources including labor force and natural resources (Cavusgil et al., 2002, pp. 1-5).

“Risk is a little word but it looms large over the emerging market space” (Marr & Reynard, 2010, p. 41). According to 2013 data, 85 percent of global population lives in emerging markets, 90 percent of it being younger than 30 years old (Boumphrey & Bevis, 2013). In emerging markets a growth of population is expected to be three times larger than the one in developed countries, which gives potential for future economic growth of emerging economies (Boumphrey & Bevis, 2013). The trend favorable to emerging and developing markets is forecasted until 2020. Euromonitor predicts that the world’s five largest economies in 2020, measured in Purchasing Power Parity terms (PPP) will be:

Table 1.

<table>
<thead>
<tr>
<th>Rank</th>
<th>Country</th>
<th>GDP in PPP: 2020 (in Billion USD)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>China</td>
<td>26,117</td>
</tr>
<tr>
<td>2</td>
<td>USA</td>
<td>22,482</td>
</tr>
<tr>
<td>3</td>
<td>India</td>
<td>9,297</td>
</tr>
<tr>
<td>4</td>
<td>Japan</td>
<td>5,620</td>
</tr>
<tr>
<td>5</td>
<td>Russia</td>
<td>4,410</td>
</tr>
</tbody>
</table>

The emerging markets and the returns experienced there are more subject to political risk than the developed markets (Diamonte, Liew, & Stevens, 1996). Historical evidence indicates that the risks faced by various businesses have been the highest when investing to developing markets due to unstable political systems. According to the research done by the “Water House Coopers” in 2001, unclear policy making environment is comparable to an increase in taxation of at least 33 percent (Henisz and Zelner, 2011).

The authorities of emerging markets have noticed “that more value can be extracted from foreign enterprises through the more subtle instrument of regulatory control rather than outright seizures” (Henisz and Zelner, 2011).

To conclude, even though emerging markets are still more subject to political instability than developed Western economies, they also provide businesses with abundant opportunities (Cavusgil et al., 2002). Major shifts in the economies of developing countries have been taking place for a while. Businesses also have improved or changed their strategies in front of political risks.

4. Emerging market of Russia and political risk

Russia is a geographically largest country in the world with around 142.7 million inhabitants (Countrysmeters, 2014). Russia is a major consumer market in the region, which accounted for 49.3 percent of total consumer expenditure in 2013 (Hodgson, 2014). It is an important emerging market for investors. The World Bank’s Doing Business of 2014 rank Russia 92nd out of 189 states (benchmarked to June 2013) improving remarkably from 111th out of 185 countries in the previous year’s report (World Bank, 2014). Hence, with an increasing political tension, the economic situation is affected as well. In particular, with the escalation of the Russian - Ukrainian conflict, measures taken by the international society are getting harsher, setting hurdles for investments made in Russian market. The EU sanctions against Russia have been imposed in several steps. Currently the new measures are on their way because Russia has basically ignored all the sanctions and introduced its sanctions on the EU member states. Consequently, there is yet no solution for the current state of affairs. Some analysts and politicians descrive such situations’ development as a all involved-sides political risk?

The divergence of opinions among the leaders of the European Union is significant and leads to complicated decision-making. This feature is not that easy to overcome under the current circumstances of Russian - Ukrainian tension too. The EU policy process based on compromise and bargaining is revealing itself as a cumbersome feature when willing to fight back the Russian policy. For instance, Lithuanian authorities declare to support stricter sanctions on Russia while Germany, Italy, France have a more careful position on this matter.

Due to the conflict between Russian Federation and Ukraine, the sanctions are imposed on Russia and they are starting to show effect on Russian economy (Verma, 2014). In addition, investors are taking their money from Russia and it is worsened by the Ukrainian crisis. The highest drop (by almost a third) in pre-tax profits was reported in January of 2014 (Reuters, 2014). The European Central Bank says capital flight from Russia since the Ukraine crisis erupted may be four times higher.
than admitted by the Kremlin, a clear sign that sanctions pressure is inflicting serious
damage on the Russian economy (Evans-Pritchard, 2014). Mario Draghi, the ECB’s
president, said the outflows from Russia have been large enough over recent time to
push up the euro exchange rate, complicating monetary policy for the ECB. “We had
very significant outflows that have been estimated by some to be in the order of
€160bn out of Russia,” he said, without specifying where the information came from
(Evans-Pritchard, 2014). Moody’s Investors Service has downgraded the government
of Russia’s debt rating by one notch to Baa2 from Baa1 at 17th October 2014
(Moody’s, 2014).

To sum up, Russia - one of the largest markets in the World - is currently facing high
economic dangers due to a very sensitive and hazardous political environment,
followed by sanctions from Western countries, including the European Union and the
USA.

According to the “European bank for Reconstruction and Development”, food import
makes up to 10 percent of all the imports to Russia, one third of food import being
from the EU member states. The ban on food import from the European Union
member states and some other Western economies will not harm only them. Russia
is also subject to negative consequences - the ban will disorder well established food
supply channels and lead to elevated import prices resulting in higher inflation
(Markovic, et al., 2014).

The amount of around 6.7 billion Euros of the EU production is linked to Russian
demand for food products. It is 6 percent of total production of the European Union or
in other terms, 0.4 percent of EU GDP (ING Bank, 2014).

Russia after Western sanctions have started to promote so called import substitution
policy, i.e. to wide and develop trade relations with countries, which probably won’t
join to mentioned sanctions, such as BRIC partners (Brazil, China, India), also
Turkey, Belarus, Serbia, South Africa. Will these countries get benefit from widening
trade flows with Russia? Will Russia really substitute all necessary food products?
Obviously, it will be quite clear in near future, but also it depends on economical
effectiveness of such factors as transport costs, and logistic challenges related to
foodstuffs, as well as production capacity of these economies to accommodate large
Russian market. The share of some imported food sales in Russia (also the main
categories in Lithuanian export to Russia) is quite high (Table 2.)

Table 2. Imported share of some goods’ sales in Russia, 2013, in per cent

<table>
<thead>
<tr>
<th></th>
<th>Cheese</th>
<th>Milk &amp; Cream</th>
<th>Butter</th>
<th>Meat &amp; Poultry</th>
<th>Meat products</th>
<th>Oils</th>
</tr>
</thead>
<tbody>
<tr>
<td>Source</td>
<td>Markovic, et al., 2014</td>
<td></td>
<td></td>
<td></td>
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</tr>
</tbody>
</table>

We can see reflection of dominated food products in sales in composition of Russian
food consumption, that is very important for a proper evaluation of potential
difficulties in supply of mentioned categories and for estimating connected political
tension.
Table 3. Composition of Russian food consumption, in per cent

<table>
<thead>
<tr>
<th>Meat products</th>
<th>Meat</th>
<th>Dairy</th>
<th>Sweets</th>
<th>Fruits</th>
<th>Vegetables</th>
<th>Fish, seafood</th>
<th>Others</th>
</tr>
</thead>
<tbody>
<tr>
<td>17</td>
<td>13</td>
<td>12</td>
<td>12</td>
<td>6</td>
<td>7</td>
<td>7</td>
<td>7</td>
</tr>
</tbody>
</table>

Source: Markovic, et al., 2014

The effect of sanctions on Russian GDP is likely to be negative overall. Some initial positive GDP effect may come from increased domestic food, and in some way it could help in developing of domestic industries. But, a 4 per cent increase in domestic food production can only make up for around 15 per cent of food imports (Markovic, et al., 2014). The negative effects may be partly mitigated in the short term through use of inventories and if alternative suppliers are found quickly.

5. Emerging market of Lithuania and food industry

The Global Competitiveness Index 2014-2015 indicates Lithuania in the 37th position. On the institutional dimension it is ranked 58th (World Economic Forum, 2014). Hence, there is space for improvement in order to make Lithuania more competitive and enhance business environment. Regarding the business environment, the overall “Ease of Doing Business” rank puts Lithuania in the 17th position - that is an improvement of 8 places in comparison to 2013 (World Bank Group, 2014).

Lithuania is one of the EU member states that have most at stake when talking about the trade with Russia. According to the Figure 1 indicated below, export to Russia composes a major part of overall Lithuanian exports. 25.4 percent of services are exported to Russia while even 42.7 percent of good are re-exported from Russian market. In addition, 7.1% of Lithuanian origin goods (excluding mineral products) are exported to Russia.
Figure 1. Key exports markets of Lithuanian goods and services


Food is a product which Lithuanian producers export most. In 2013 Lithuanian origin exports of agriculture and food processing products to Russia composed almost a half (46 percent) of all the Lithuanian export to the Federation of Russia (see Figure 2).

Figure 2. Structure of Lithuanian origin export to Russia, in per cent

In 2013, from Lithuanian agricultural products export to Russia, dominated fruits and vegetables, dairy and eggs, and all these categories included in the “black list” of sanctions. Lithuanian export of food and beverages to Russia in 2013 reached 1,8 bln USD.

The vegetables/fruits export sector appears particularly vulnerable as three quarters of these exports are shipped to Russia. The overall GDP effect appears to be less potent in other sanctioned economies where shares of food export to Russia are less than half a percentage point of GDP.

As to Russian officials and related business media, “embargo will cost for Lithuania 0,4 percent of Lithuanian GDP in 2014”. And the most sensitive categories from food industry will be vegetables and fruits. (Vestifinance, 2014).

Table 4. Food export shares to Russia

<table>
<thead>
<tr>
<th>Country</th>
<th>Percent of total exports</th>
<th>Percent of GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lithuania</td>
<td>3,89</td>
<td>2,72</td>
</tr>
<tr>
<td>Estonia</td>
<td>0,5</td>
<td>0,36</td>
</tr>
<tr>
<td>Latvia</td>
<td>0,75</td>
<td>0,34</td>
</tr>
<tr>
<td>Norway</td>
<td>0,64</td>
<td>0,2</td>
</tr>
<tr>
<td>Poland</td>
<td>0,54</td>
<td>0,2</td>
</tr>
<tr>
<td>Hungary</td>
<td>0,16</td>
<td>0,13</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>0,10</td>
<td>0,05</td>
</tr>
<tr>
<td>EU 28</td>
<td>0,13</td>
<td>0,04</td>
</tr>
<tr>
<td>Canada</td>
<td>0,14</td>
<td>0,03</td>
</tr>
<tr>
<td>Cyprus</td>
<td>0,4</td>
<td>0,03</td>
</tr>
<tr>
<td>Australia</td>
<td>0,12</td>
<td>0,02</td>
</tr>
<tr>
<td>Slovakia</td>
<td>0,02</td>
<td>0,02</td>
</tr>
<tr>
<td>Croatia</td>
<td>0,07</td>
<td>0,01</td>
</tr>
<tr>
<td>US</td>
<td>0,09</td>
<td>0,01</td>
</tr>
<tr>
<td>Slovenia</td>
<td>0,01</td>
<td>0,01</td>
</tr>
<tr>
<td>Romania</td>
<td>0,00</td>
<td>0,00</td>
</tr>
</tbody>
</table>


When export figures from the most affected CSEE countries to Russia are collated with imports of the same products from other EU-28 countries, it emerges that substantial portions of the exported foodstuffs may be imported from other EU countries, may be shared with other producing countries within the EU.
Table 5. Exports shares to Russia in total import from the EU-28

<table>
<thead>
<tr>
<th>Country</th>
<th>Meat</th>
<th>Dairy</th>
<th>Fish</th>
<th>V&amp;F</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lithuania</td>
<td>30.4</td>
<td>59.5</td>
<td>3.3</td>
<td>68.5</td>
<td>53</td>
</tr>
<tr>
<td>Poland</td>
<td>8.3</td>
<td>20.7</td>
<td>0.7</td>
<td>43.8</td>
<td>20.3</td>
</tr>
<tr>
<td>Latvia</td>
<td>5.3</td>
<td>21.1</td>
<td>26.2</td>
<td>3.7</td>
<td>12.2</td>
</tr>
<tr>
<td>Hungary</td>
<td>17.7</td>
<td>2.8</td>
<td>0.0</td>
<td>10.4</td>
<td>11.3</td>
</tr>
<tr>
<td>Estonia</td>
<td>3.3</td>
<td>39.1</td>
<td>8.2</td>
<td>2.5</td>
<td>10.4</td>
</tr>
</tbody>
</table>


Lithuanian food industry always have been connected with Russian market, and not the first time experienced political risk. Business enterprises have to define and manage such risk properly as it possible in every new given situation. Not be forgotten that in the periods of less risky environment these producers are getting bigger profits from such market as Russian, and as a fact such higher risk brings also bigger losses, as it is a wellknown risk rule. Taking that position, some Lithuanian business representatives loud requirements to state authorities to help them or with interventions – buying their food products, i.e. diary, cheese etc. for budget account, or dotations to cover their losses, also from budget, to put it mildly are absolutely unfounded.

Other reason, to take and put efforts to manage such political risk, is a big potential of Russian emerging market, that is can not be ignored and in better way could bring future bigger incomes. So, present situation contrast political risk against growing investment possibilities, and probably in the best scenario all parties will find risk management methods.

6. Forecast and opinions

Recently economists and related organizations have published recalculated forecasts for the economy of Lithuania in reference to new developments regarding the Russia - Ukraine conflict and sanctions imposed.

The Central Bank of the Republic of Lithuania currently forecasts Lithuanian GDP to grow 0.4 percent less than declared earlier - by 2.8 percent in this year and 3.3 percent in 2015. As the domestic demand is still on the increase, the projections of the economy are not worsened as much as may have been (Central Bank of the Republic of Lithuania, 2014).

The Swedbank analysts claim that the growth of Lithuanian economy will be slower but the effect of sanctions will be limited. The possibility of worsening geopolitical situation and increasing political risk is an important factor which will probably limit both the investments and economic expectations (Swedbank, 2014).

The analysts of SEB bank forecast a GDP growth of 2.7% in a second half of 2014 - their prognosis stays the same, however the growth in 2015 is diminished from 3.8% to 3.2% (SEB group, 2014). In addition, DNB bank also decreased the forecasted growth from 3.5% to 3% in 2014 (DNB, 2014).
The analysis of official reports as well as various articles and interviews provides that the authorities of Lithuania are actually employing Russia, our common threat, image and highlighting economic sanctions as a way to diminish some points regarding domestic politics. For instance “Lithuanian Confederation of Industrialists” agree with the fact that difficult relations complicate the economic situation of Lithuanian businesses, however, they do underline that government should put more efforts to improve business environment in Lithuania rather than put most energy on other matters related to foreign affairs (Verslo zinios, 2014).

On the 20th of August of 2014 the Government of Lithuania proposed the recommendations regarding the search for new markets available for exports as an answer to the sanctions imposed by Russia on the imports of some products (The Government of the Republic of Lithuania, 2014). These main tools are recommended in order to diversify export and find new markets: first, setting five main alternative markets for export of agriculture, food products and the sector of transport, second, organizing participation in various exhibitions, business missions and similar events, third, providing businesses with market research data and consultations on a search of new business partners (The Government of the Republic of Lithuania, 2014). Other tools include financial support and include, for instance, providing enterprises with additional funding of 7 million litas for international projects, also offering loans at lower interest rate for the companies harmed by sanctions. It is decided to ask European Commission for permission to purchase an oversupply of agricultural products and take other regulatory measures (The Government of the Republic of Lithuania, 2014).

The data of “European Bank for Reconstruction and Development” indicates Lithuania as a state which will probably experience a major effect of a loss of Russian market: Lithuania has a biggest share of food export to Russia as a percentage of GDP in comparison to other countries worldwide (Markovic, et al., 2014). It is claimed that a substantial part of Lithuanian exports to Russia are re-exports from Western economies (may be up to 80 percent) rather than export of domestically produced food products (Markovic, et al., 2014). Consequently, the domestic food production in Lithuania should not be affected that much - at least less than other dependent on Russian economy sectors, for instance, transport sector (Markovic, et al., 2014).

Furthermore, the European Commission states that risks to growth are decreasing and on the domestic side recovery advances. However, with the improvement of domestic situation the necessary reforms may be delayed and slow down the further advancements. Moreover, external markets, particularly, emerging ones, are still subject to risks and uncertainty about growth prospects. It is highlighted that the situation with Russia has increased the geopolitical risks (European Commission, 2014).

7. Conclusions

Political risk is traditionally counted as non-manageable, speculative, and as a fact is mostly only formally integrated into Enterprise risk management, describing it in one or another manner in company’s Risk Policy or Risk management programme.
Political risk has a substantial influence on businesses which enter emerging markets as it is long term affect most often. However, companies may aim at manage risk to at least diminish company’s exposure to uncertainties. It is important provided that emerging markets, including the politically risky ones, may present business opportunities worth exploiting. In other words, some companies still enter the emerging markets subject to political uncertainty. As a result, there should be a reward in the market. In other words, taking risk but not expecting the return on investment is never a case for a profit seeking business.

Around the year 2000 some major shifts in economies of developing countries took place. To start with, risks of doing business in developing countries have become more manageable. Also, instead of being simply technologically as well as economically behind emerging markets have experienced larger growth of income in comparison to developed economies, they also have become more competitive technologically. In addition, consumers in emerging markets have increasing purchasing power, which offers more opportunities for businesses. Furthermore, emerging markets are large markets which offer low-cost, in some countries even abundant resources including labor force and natural resources (Cavusgil et al., 2002, pp. 1-5).

Russia - one of the largest emerging market - is currently facing high economic dangers due to a very sensitive and hazardous political environment, followed by sanctions from Western countries, including the European Union and the USA.

According to the “European bank for Reconstruction and Development”, food import makes up to 10 percent of all the imports to Russia, one third of food import being from the EU member states. The ban on food import from the European Union member states and some other Western economies will not harm only them. Russia is also subject to negative consequences - the ban will disorder well established food supply channels and lead to elevated import prices resulting in higher inflation.

The effect of sanctions on Russian GDP is likely to be negative overall. Some initial positive GDP effect may come from increased domestic food, and in some way it could help in developing of domestic industries. But, a 4 per cent increase in domestic food production can only make up for around 15 per cent of food imports (Markovic, et al., 2014).

Lithuania is one of the EU member states that have most at stake when talking about the trade with Russia. Export to Russia composes a major part of overall Lithuanian exports. 25.4 percent of services are exported to Russia while even 42.7 percent of good are re-exported from Russian market. In addition, 7.1% of Lithuanian origin goods (excluding mineral products) are exported to Russia.

Food is a product which Lithuanian producers export most. In 2013 Lithuanian origin exports of agriculture and food processing products to Russia composed almost a half (46 percent) of all the Lithuanian export to the Federation of Russia.

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sanctions. Lithuanian export of food and beverages to Russia in 2013 reached 1.8 billion USD.

Lithuania as a state which will probably experience a major effect of a loss of Russian market: Lithuania has a biggest share of food export to Russia as a percentage of GDP in comparison to other countries worldwide.

The European Commission states that external markets, particularly, emerging ones, are still subject to risks and uncertainty about growth prospects. It is highlighted that the situation with Russia has increased the geopolitical risks.

To sum up, statistical data indicates that Lithuanian food sector has a major interest in Russian market – Lithuanian food export to Russia has the biggest share of GDP in comparison to other countries affected by the sanctions. Thus, the complaints of Lithuanian food exporters may not be called having no background. On the other hand, re-exports have a major share of Lithuanian food exports, hence, the Lithuanian producers directly should not be affected as much in current situation, but in case if some new related sanctions would be imposed, influence on food industry could bring greater political risk, if not uncertainty.

References


