

World Potash Market:

World potash demand has improved in recent years, to the benefit of all potash suppliers, including those in Russia and Belarus. However, trade flows could be disrupted in the near future, fears Mr. Alexey Litvyakov, Deputy Director General at International Potash Company (IPC), if the EU decides to strengthen its stance on imports of potash from Russia and Belarus.

STRONG POTASH MARKET IN 2004

2004 proved to be another year of strong market demand for the potash sector. World potash production and trade rose by 11% and 10% respectively. Global trade volumes exceeded total production and stocks were drawn down, a sure sign of increasing world demand. Potash imports increased substantially, rising by about 9.8% above the level of 2003 and totaling around 25.5 million K₂O. IPC exports followed the world trend, rising to about 10 million tonnes product. Major increases in deliveries were registered to a number of major consumers in Asia, notably China, Indonesia, Malaysia and India; imports also increased in North America (USA), Latin America and Central Europe. Western Europe was the only region that experienced a decline in imports. The healthy market environment ensured higher utilization rates within the potash industry, production rising to 82% of nameplate capacity compared with 76% in 2003 and bringing the sector closer to a supply-demand balance.

GOOD START TO 2005

Early 2005 trends have also been positive for the potash industry, despite some concerns. The slowdown in import demand witnessed in Brazil at the end of 2004 continued in the first quarter of 2005; this primarily resulted from a slump in soya bean prices and a relatively high carryover of stocks. Unfavourable weather conditions, namely drought, negatively affected import demand in some markets in South-East Asia. However, the adverse effects were more than offset by buoyant demand from a number of key import markets, such as China and India, which have concluded large contracts for potash supplies for 2005. In addition, Eastern European markets also demonstrated sustained interest in potash deliveries during the first three months of the year. So, despite a lull in import activity from consumers in Latin America and some in South-East Asia, the market has remained stable.

We believe that the positive tone of the market beginning in 2003 and continuing into 2004 will persist this year. Improved soya bean prices are supposed to eventually prompt a revival of import demand in Brazil. South-East Asia is also expected to return as an active importer once climatic conditions improve. However, trends in import demand will undoubtedly vary between markets with local factors that affect the market environment in

individual nations/regions. On the whole, world potash consumption is projected to rise by about 3% this year, similar to the level forecast by IFA for 2004. This is in line with the general trend in world fertilizer consumption, which is forecast to grow at an annual average rate of around 2.1% over the next four years. This upward movement in fertilizer consumption will be supported by a satisfactory world GDP growth rate of about 4.3% and current positive developments in agricultural markets. In addition, the ever-rising world population and the promotion of intensive agriculture are additional indirect factors that will encourage higher potash fertilizer demand.

RISING COSTS IN RUSSIA AND BELARUS

In general, the macroeconomic indicators that affect the world potash fertilizer market remain the same. The same is also true of the potash industry in Russia and Belarus. The approaching accession of Russia and Belarus into the WTO has prompted a liberalization of prices for natural gas and energy tariffs, which are raising the costs of production for potash producers. In 2004, higher gas prices and energy tariffs were among the reasons that led to an increase in consumer prices and inflation in the region, with inflation reaching 11.7% in Russia. These economic forces, along with a weaker US dollar and increasing transportation expenses in terms of railway tariffs and freight rates, are putting considerable pressure on the netbacks for Russian and Belarus potash. Last year, the exchange rate of the Russian Rouble against the US dollar increased by 14%, while railway tariffs in Russia rose by 12%. During the fourth quarter of 2003 and the first quarter of 2004, freight rates doubled.

The prices of Russian and Belarus potash have to be structured to help the producers in these countries to offset ever-increasing cost levels throughout the potash production/distribution chain. So, in the first and second quarters of 2005, price levels for Russian and Belarus potash were raised. The revenue from exports is still the main source of investment funds for the Russian and Belarus potash producers. A drastic reduction in profits would result in cuts in the funding needed to finance required investment programmes in production and logistics. At present, JSC Silvinit, Russia, is implementing a four-year plan, scheduled for end-2008 completion, which, above all, includes a major overhaul of its production facilities and the purchase of

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specially-designed railcars. In addition, the producer is involved in the construction of a terminal at the port of Nikolayev. PA Belaruskali also has an investment programme in place. This commenced in 2002 and is aimed at maintaining potassium salt resources, improving ore processing technologies, putting into operation a new mine to offset the depletion of potash reserves at one of the four existing mines, and at replacing old mining and processing equipment with modern, state-of-the-art equipment. This programme is due to be completed in 2010.

Rising costs of production and escalating transportation costs, coupled with a strong market demand environment, make increasing product prices inevitable. We believe that the remainder of this year will see sustained market demand, on the one hand, and increasing prices, on the other hand. However, it is unlikely that the rate of increase will be as high as that witnessed last year.

EU REVIEWS TRADE RESTRICTIONS ON POTASH ARRIVING FROM RUSSIA AND BELARUS

EU markets are a major concern to us. Over the last ten years, potash consumption in the old EU-15 has gradually declined as a result of the implementation of the Common Agricultural Policy (CAP). This contrasts with trends in potash demand in East European markets, though total use in these nations is lower than in the old EU-15. Since 2000, potash demand in Eastern Europe has steadily increased in line with world consumption. In fact, over the last four years, potash consumption in Eastern Europe has increased by 28.5%. This growth is expected to continue as accession to the EU means that farmers in the new EU-10 will be entitled to agricultural subsidies, as granted to farmers in other EU member states. A portion of these subsidies will most definitely be spent on fertilizer as they are a highly cost-efficient method of raising yields and production. Traditionally, potash from Russia and Belarus has accounted for 90% of total potash supplies to the new EU-10 markets.

However, last year, as a transitional measure, undertakings were enforced that allowed Russia and Belarus to supply potash to the new EU-10 nations on the basis of quotas and a minimum import price. Unfortunately, the quantities that can be made available by the producers in Russia and Belarus under the terms of these restrictions are insufficient to meet the demand of the new EU-10 markets. In May 2005, a revision to the current trade restrictions is

anticipated. The terms of this revision are uncertain. It may be that the trade restrictions that currently apply to potash from Russia and Belarus in the old EU-15 may be extended to cover potash shipments from these suppliers to the new EU-10. In 1992, potash supplies from Russia and Belarus to the old EU-15 markets were restricted when anti-dumping duties were imposed; since 1994, practically prohibitive duties have been applied on potash from these sources entering the old EU-15. This is due to continue until 20 May 2005, by which time a decision will have been taken on whether to prolong or amend the current restrictions. On 13 April, the EU initiated an expiry review of the anti-dumping duties on potash imports from Russia and Belarus and separately announced that a partial interim review would take place of the anti-dumping duties on potash imports from Belarus. The same procedure was put in place last year in relation to Russian potash.

Though it is difficult to predict the outcome, we are optimistic. In our opinion, tighter customs regulations on potash imports from Russia and Belarus are of no benefit to local

agricultural producers. Such regulations would reduce potash supplies to the new EU-10 markets as anti-dumping duties would make deliveries of Russian and Belarus potash to these states economically unviable; consequently, product would have to be redirected to other markets outside the new EU-10. Also, it would be difficult for the European potash manufacturers to satisfy all of the potash demand of the new EU-10. To do so, they would have to cut back on their exports outside of the EU, cease supplying some offshore markets entirely and, as application seasons in the old EU-15 and the new EU-10 coincide, they would have to invest in considerable additional potash storage capacity.

We hope that the new decision on potash imports from Russia and Belarus will not affect the existing trade structure with the new EU-10, which has been in force for many decades. We are certain that a solution can be found that will be beneficial to both the potash consumers in the EU and the Russian and Belarus potash producers. ■



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