2022 Russian invasion of Ukraine: A war fought over 7,000km away but with casualties in Kenya

At a glance:

1. **The genesis of the Russia-Ukraine conflict is a geopolitical standoff between the North Atlantic Treaty Organization (NATO) and the Russian Federation over Ukraine's intention to join NATO.**

2. **Russia is classified as one of the world's largest producers and exporters of oil and gas, metals and minerals as well as chemical fertilizers. It is also a significant player in cereals and grains in the global economy. Equally, Ukraine is a major exporter of grains in the world market. Over the years, Kenya has imported goods such as cereals, oilseeds and seeds, animal/ vegetable fats and oils from Ukraine.**

3. **Kenya is the fourth largest trading partner with the Russian Federation in Sub-Saharan Africa after South Africa, Senegal, and Nigeria. The total volume of trade between Kenya and Eastern Europe is approximated at Kshs. 59,591 million with a trade deficit of Kshs 33,407 million in favour of the Russian Federation as of 2020.**

The Ukraine-Russia war could plunge the global economy into a new crisis, exacerbating an already weak economic recovery. At the beginning of the year, even before the war started, the IMF had revised its global economic growth projection[1] downwards by half a percentage point to 4.4 percent. This was informed by lingering effects of the pandemic, disruption of the global supply chain as well as rising cost of crude oil, fertilizers and other vital commodities[2]. The Russia – Ukraine conflict presents a more ominous risk to the performance of the global economy primarily due to disrupted trade and supply chains. Indeed, taking into account the likely impact of the war, the IMF has already revised its global economic growth projection further downwards to 3.6 percent in 2022. This is 0.8 percentage points lower than the January forecast.[3]

Russia is classified as one of the world's largest producers and exporters of oil and gas, metals and minerals as well as chemical fertilizers. It is also a significant player in cereals and grains in the global economy. On its part, Ukraine is a major commodity producer particularly of wheat and corn; and, jointly with Russia, accounts for approximately 29% of global wheat exports. In addition to wheat, Ukraine and Russia are both major exporters of some of the world's most basic foodstuffs; 19% of global corn supplies and 80% of global sunflower oil exports. African countries rely heavily on these two countries in terms of wheat production and consumption. Statistics indicate that East African countries import 90 percent of their wheat from Russia and Ukraine.

Ukraine further plays a critical geo-economic role to both Europe and Russia; providing critical infrastructure including a complex network of natural gas pipelines and motorways that transport goods by road from Russia to Europe and vice versa. Disruptions along this trade and energy flows corridor will therefore have significant implications not only in Europe but also across the globe.

The impact of the sanctions imposed on Russia is already being felt across the globe primarily through food and energy prices. The sharp increase in the price of oil and gas can be directly linked to uncertainties surrounding the Russia-Ukraine conflict including decisions by some key players in the oil industry to shun the Russian oil market in order to avoid legal and reputational risk[4]. With regard to food exports, there has been a

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[1] **IMF – WEO update for October 2021 projection**
[2] **IMF-WEO update for January 2022**
[3] **IMF-WEO April 2022, Global economic outlook, War sets back the Global Recovery**
[4] **Kalish, I (2022). How sanctions impact Russia and the global economy. Deloitte Insights. Retrieved from https://www2.deloitte.com/us/en/insights/economy/global-economic-impact-of-sanctions-on-russia.html**

notably increase in the prices of wheat and corn of which Russia and Ukraine are key exporters. More ominously, a prolonged conflict in the region may trigger a global food crisis.

WILL KENYA BE CAUGHT IN THE CROSSFIRE?

Though the Kenyan economy has been on a recovery trajectory from the adverse effects of the Covid-19 pandemic; it was already facing significant headwinds from the prevailing drought conditions, election related uncertainties, as well as the high cost of fuel, food items and agricultural inputs which have led to an increase in the cost of living. Over and above these internal risks, the Russia-Ukraine conflicts presents a major external risk to this recovery process and may contribute to a significant slowdown in growth. (Current projected economic growth is at 4.9 percent[5] in 2022).

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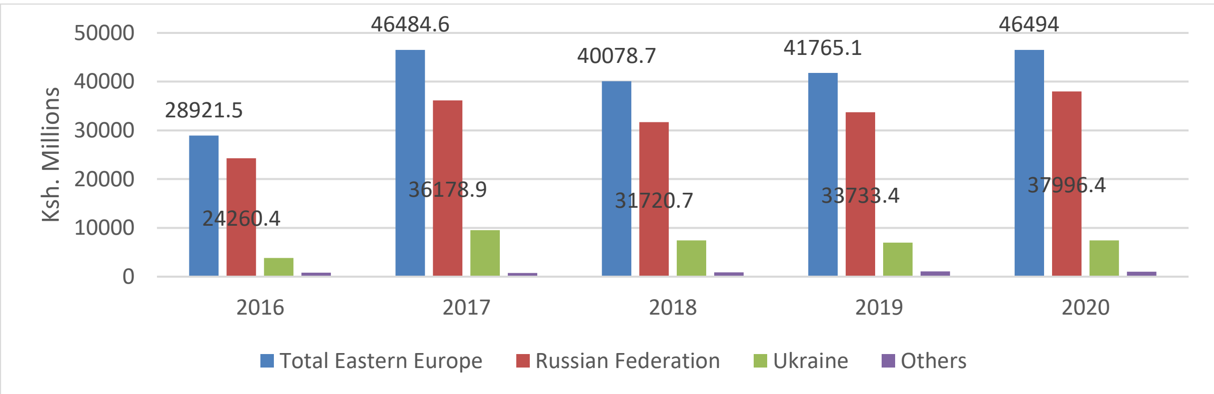
Kenya relies on the Russian Federation for import of wheat, fertilizers, iron and steel, and paper. According to the KNBS, Kenya's imports from Eastern Europe grew significantly from 4 percent in 2019 to 11 percent in 2020. This growth was on account of increased import demands of Iron and Steel from the Russian Federation. Russia is the biggest contributor of exports to Kenya from Eastern Europe, accounting for 81 percent of total imports to Kenya from this region on average (Figure 1). Equally, Ukraine is a major exporter of grains in the world market and over the years, Kenya has imported cereals, oilseeds and seeds, animal/ vegetable fats and oils from Ukraine.

Figure 1: Values of Imports to Kenya from Eastern Europe (2016-2020)



Source: Economic Survey 2021

The Russia- Ukraine conflict and the economic sanctions against Russia are likely to disrupt these trade linkages and supply chains leading to shortages in the market and an exponential increase in prices of these commodities. Notably, the construction sector is likely to feel the impact due to a likely shortage of iron and steel. Recent reports indicate that the construction sector is already facing challenges due to an **exponential increase in prices of cement, iron sheets and deformed steel bars**. This cost is attributed to high taxation,

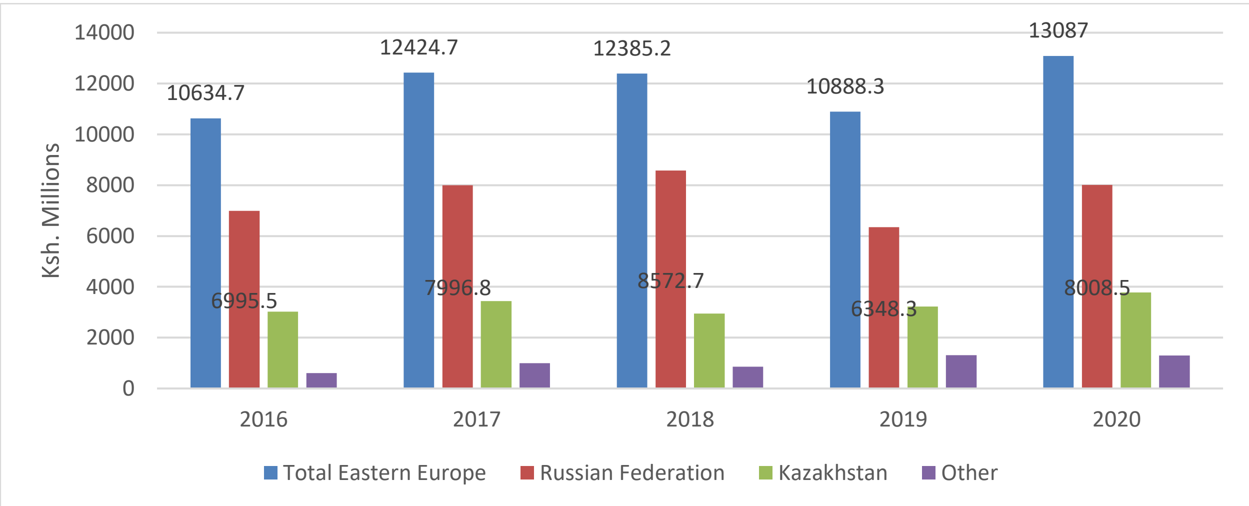
[5] **PBO projection**

high cost of electricity, high fuel cost and rising global costs of raw materials[6] such as clinker which is used in cement production and iron ore which is a key ingredient of steel. Furthermore, China, the world's top steel producer has capped its crude steel output on account of timelines to achieve peak carbon emissions as well as reduced internal steel demand. This could be a significant contributor to the prevailing steel price volatility. If trade with Russia is disrupted, the impact on the construction sector will be significant. Evidence already indicates that the Russia-Ukraine conflict is contributing to a global surge in steel prices. If the trend continues unabated, many construction activities are likely to slow down significantly or stall altogether. This is especially significant for individual construction/housing projects, most of which are facing significant losses and will most likely stall. Government infrastructure projects particularly in roads sector and also on affordable housing will be particularly affected.

Other goods whose supply and prices are likely to be affected include wheat and other cereals as well as fertilizer.

Kenya exports cut flowers, tea, fruits and vegetables to Russia, Ukraine and the rest of Eastern Europe. Indeed, Russia is among the top 5 importers of Kenya coffee while Ukraine, Poland and Kazakhstan are emerging new markets. Although the growth of exports to Eastern Europe recorded a negative performance of 12 percent in 2019, it rebounded by 20 percent in 2020. Russia is the largest importer of Kenya products in Eastern Europe and the upward trajectory implies existing opportunities in the region (Figure 2). Should the conflict persist, therefore, it means that Kenya's exports in these potential markets will be substantially subdued leading to lower export earnings.

Figure 2: Values of Exports from Kenya from Eastern Europe (2016-2020)



Source: Economic Survey 2021.

Reliable, credible and globally acceptable settlement system is an integral part of international trade and global financial system stability. The delisting of some Russian banks and the possibility of full withdrawal by SWIFT (Society for Worldwide Interbank Financial Telecommunications) from the Russian Banking system as part of the wider sanctions by the European Union, will present challenges in settling of imports and exports to and from Russia. This will have far reaching impact as it may increase transactional costs for international trade or make it impossible to trade with the Russian Federation.

[6] **Nation (2022), why prices of cement, steel have doubled. Retrieved from https://nation.africa/kenya/business/why-prices-of-cement-steel-have-doubled--3770770**

IS THERE AN IMPENDING OIL CRISIS IN KENYA?

Russia is the world's second-largest exporter of oil and gas. Although Kenya primarily imports oil from United Arab Emirates (UAE), Saudi Arabia, India, China, and Malaysia, the go slow by various refineries and oil shipping companies in relation to trading with Russia makes Kenya vulnerable and increases its exposure to the crisis since the major oil importers from Russia will opt for alternative sources like UAE leading to supply shocks. A reduction in the supply of the commodity to the rest of the world has resulted in high prices of petroleum products. In the month of March, crude oil prices rose to peak at USD. 116.81 per barrel compared to USD 74.38 per barrel as the end of 2021[7].

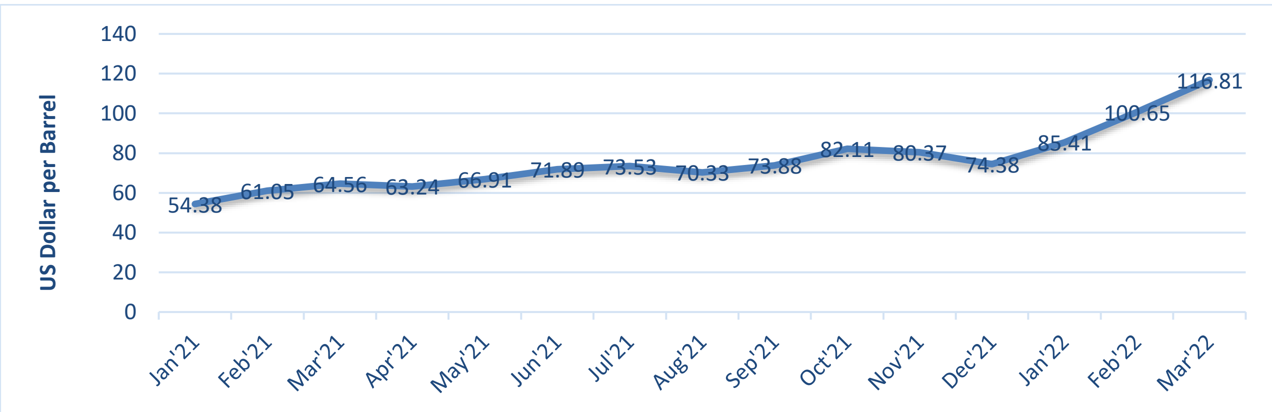
Table1: Kenya Major Oil Import origin (2018-2020)

KENYA'S MINERAL FUELS, MINERAL OILS AND THEIR PRODUCTS IMPORTS (THOUSAND US DOLLAR)			
COUNTRY	2018	2019	2020*
United Arab Emirates	1,164,580	1,362,706	583,910
Saudi Arabia	1,356,589	916,587	369,527
India	354,016	368,369	348,639
China	7,043	112,579	16,042
Malaysia	-	64,769	66,912

Source: ICT Trademap.

The energy sector is one of the key drivers of the Kenyan economy supporting the manufacturing sector and the agriculture sector which are key contributors to economic growth. Higher oil prices imply higher production costs which will invariably be passed on to the consumer leading to a higher cost of living. Going forward, the crude oil prices are expected to remain in an upward trajectory, on account of the ongoing Russia-Ukraine conflict.

Figure 3: Monthly Average MURBAN ADNOC Prices January 2021- March 2022



Data source: KNBS& CBK 2022

[7] **CBK weekly bulletin various editions**

The government has been subsidizing fuel prices to cushion against the effects of the Covid-19 pandemic. In the supplementary budget I for 2021/2022, the government allocated Kshs. 31.7 billion to the Petroleum Development Levy (which had been depleted) to cater for fuel subsidy and stabilize fuel prices due to increasing fuel prices in the country.[8] Going forward however, the outlook of higher fuel prices may render this subsidy unsustainable.

However, the crisis presents an opportunity. The global shortage of oil supplies may hasten oil exploration in other parts of the world, including Kenya. This puts Kenya on the right track in terms of attracting the best technology and innovations to exploit the oil deposits in larger areas of Northern Kenya. Currently, the oil discovered in Turkana 10 years ago has not borne any significant impact to Kenyans and remains untapped after years of delayed investment commitments. Attracting more investors and with competing new technology will be a game-changer. This will result in high economic growth, as well as job opportunities for Kenyans and, eventually, an increase in per capita income. Fuel price stability will be achieved, and many oil-related levies will be repealed. The government will be able to direct its spending toward more impactful public expenditures while also aiming to save money.

DOUBLE EDGED SWORD FOR THE AGRICULTURE SECTOR

Russia, Ukraine, Belarus, and the Baltic states are key suppliers of fertilizer to Kenya and the global market. According to the World Integrated Trade Solutions platform, Russia accounts for 18% of exports in potassium-based fertilizers, 20% of ammonium exports, and 15% of urea exports to the global market. The emerging crises between the Russian Federation and Ukraine will therefore result in a severe supply-side shock leading to an exponential increase in fertilizer prices.

Indeed, Russia has already announced a nationwide ban on the export of fertilizers among other commodities as retaliation to mounting global pressure and sanctions by the pro-NATO countries. The resultant prohibitive cost of this input means that the agriculture sector will suffer on two fronts: reduced access to fertilizer will lower agricultural production; and high cost of production will render Kenya's agricultural products uncompetitive in the market. Furthermore, Kenya's inability to access the Eastern European markets will lead to a significant loss of export earnings.

The price of various fertilizers in Kenya and globally, has more than doubled since the beginning of 2022; attributed to the slower recovery of the production systems amidst sharp demand growth globally. If the situation persists and without viable alternatives, low production in the agriculture sector may lead to loss of jobs in the agricultural value chains as well as underperformance of other agriculture support sectors such as agrochemicals and farm equipment. This, coupled with the already prevailing challenges in the agriculture sector such as drought, may lead to lower than expected economic growth thereby dampening expected revenue collections.

SUPPLY AND COST OF WHEAT

Wheat is arguably one of the most important cereals. According to the Food and Agriculture Organization, it accounted for roughly 27 percent of all cereal grains produced globally between 2018 and 2020. Its production is expected to reach 769.6 million tonnes in 2021, accounting for 27.6 percent of total cereal production worldwide (FAO,2021).

In Kenya, wheat is the second most important cereal after maize and its demand has increased significantly in recent years, due to an increase in both home and industrial baking. According to data from the Ministry of Agriculture, Kenya's wheat consumption currently stands at 900,000 tonnes per year, compared to a local production average of 350,000 tonnes per year. As such, domestic wheat production only meets approximately

[8] **The National Treasury submission on Supplementary Estimates 1 for FY 2020/21**

one-third of demand, thereby necessitating imports. The gap in supply is typically met by the Black Sea region (Russia, Ukraine, and Kazakhstan).

Available data from the Global Agriculture and Information Network (GAIN) 2019 indicates that in 2018, Russia and Ukraine accounted for 59.3% of the total wheat imported to Kenya (Table 2).

Table 2: Kenya Wheat Importation in Metric Tonnes per Origin

Year	Import from Russia	Import from Ukraine	% Import from Russia	% Import from Ukraine	Total Imports from Russia and Ukraine
2016	454,152	150,061	33.3%	11.0%	44.4%
2017	439,462	212,628	23.7%	11.5%	35.2%
2018	838,276	191,156	48.3%	11.0%	59.3%

GAIN: 2019

It is noted that even before the conflict, wheat prices were rising due to pandemic-related supply-chain snags and severe weather. As global consumption increased post-pandemic, wheat supply was expected to decline even further. The Russia-Ukraine conflict has therefore worsened an already precarious situation. Already, in the first quarter of 2022, wheat prices recorded a high increase following shipment disruption and imposition of a higher duty of export by Russia to protect the local markets. A prolonged conflict may lead to even more restrictions, including export bans on wheat and other grains in order to support domestic food needs. This is likely to disrupt the supply of grains, thus making them even costlier. Kenya's over-reliance on wheat imports from Russia and Ukraine will therefore prove costly and may necessitate consumption of substitute goods.

IMPLICATIONS ON TOURISM SECTOR

The National Tourism Blueprint 2030, the transformational framework for the tourism sector, identified Eastern Europe as a potential and alternative source of tourists. As such, the Kenya Tourism Board in collaboration with other government agencies has been undertaking popularization initiatives in Russia, Ukraine, Poland, Belarus, and Czech among others. As a result, there has been an increase in the inflow of tourists from these alternative destinations. For instance, the introduction of charted planes from Poland and Ukraine, which also brings travel agents and journalists from these countries as well as advertising campaigns, has significantly increased tourist arrivals from these countries. The sector was also expected to benefit greatly from the negotiations on bilateral air service agreements for direct flights between Nairobi and Moscow. The ongoing crisis is likely to water down these efforts due to closures of airspace and uncertainties related to travel in such a time.

It is noted that the tourism sector was the hardest hit by the Covid-19 pandemic[9] with a decline in international visitor arrivals by 71.5 percent and a decline in export earnings by 43.9 percent. A decline in any number of potential tourists is therefore a significant blow to the sector.

OPPORTUNITIES

1. The increase in crude oil prices may hasten oil exploration in other parts of the world, including Kenya. This puts Kenya on the right track in terms of attracting the best technology and innovations to exploit the oil deposits in larger areas of Northern Kenya.

2. Fast-track completion of Fertilizer granulation plant located in Nakuru County with an annual capacity of 100,000 MT. This will enable farmers to have access to cheaper and tailor-made fertilizer combinations

[9] **2021 Economic Survey**

thereby boosting food and crop production. Hopefully, this will address perennial issues of food security and spur growth of agriculturally based industries.

3. Operationalization of the Strategic Food Reserve to stabilize food supply and prices as well as maintain adequate strategic food reserve. Currently, there is no strategic reserve stock. The Strategic Food Reserve Fund was wounded up in 2020.