



Project no.
513705

Project Acronym
CEEC AGRI POLICY

Project title
**Agro economic policy analysis of the new member states,
the candidate states and the countries of the western balkan**

Instrument Specific Support Action

Thematic Priority Scientific Support to Policies

D12-1 First 6-monthly report
**1. MONITORING OF AGRICULTURAL POLICY,
MARKET AND TRADE DEVELOPMENTS IN LATVIA**
2. Assessment and Outlook: Sugar sector

Start date of project: 01.05.2005

Duration: 24 Months

Organisation name of lead contractor for this deliverable :

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03.01.2006	Janis Bruneniaks	Final review, editing and addition of most recent data.

Project co-funded by the European Commission within the Sixth Framework Programme (2002-2006)

Dissemination Level

PU	Public	
PP	Restricted to other programme participants (including the Commission)	
RE	Restricted to a group specified by the consortium (including the Commission)	
CO	Confidential, only for members of the consortium (including the Commission Services)	X

1 General review

1.1 General overview of agricultural and national economy developments

Also during the first half of 2005 as in the first full year period of being EU member, general economic development trends observed during the last years prior to accession, continued to prevail:

- **economic growth** in terms of GDP reached 9.5% compared to 8.3% in 2004, although in agri-food sector the growth was only 3,8 %;
- Improvement in economic performance could be observed also through developments **in internal trade**, where retail trade growth rates in 2nd quarter of 2005 were higher – 118,4 %, compared to 10,7 % in 2004.
- further increase of **external trade** volumes, and as the most important fact to be mentioned - this was the first period since regaining independency, when export growth (37,4 % as compared to related period in 2004) exceeded the growth of imports – 24,2 %, which resulted in improved foreign trade balance –20% of GDP in the first half of 2005 as compared to 22,6 % in 2004. Agri-food sector has been one of the biggest contributors to this trend with the export and import growth rates 64% and 23,7 %, respectively in the first half of 2005.
- **credit rates** after some increase just after the joining to EU (by 2,1 % points) came back close to the levels prior the accession – 5,9 % for short term and 7,5 % for long term credits. Which, compared to the current inflation rates can contribute to further growth of demand.
- joining to the EU and the economic adjustment processes have contributed significantly to the **inflation**, where Latvia keeps the highest rates in European area – consumer prices increased by 4,5 % in the first half of 2005, where agri-food products contributed the most – with 8,6 %, while in 12 months of 2004 prices went up by 7,3 % and 10,0 %, respectively.
- As the new feature of economic development, Latvia has faced after the joining EU and its relatively free labour market; significant **labour outflow** to other EU countries should be highlighted. Even not having exact statistical indicators, according to expert evaluations, net outflow of labour force during the first year of being within EU can be estimated around 50 thsd. people (~ 5 % of total labour resources), and a good share of it comes from rural sector.

Coming back to agricultural sector, agricultural volume increased for about 7%, prices went up on average by 15% but different kind of support payments more than doubled. For that reason income from agricultural activities increased near by two times. Largely, this was single growth due to low level of the previous period.

Share of agriculture in GDP constitutes about 2.4%, however agriculture plays a significant role in employment (around 10% of employed persons in the main work) and in food supply, and, due to lack of alternative activities, it is the main working possibility in rural areas.

1.2 Overview of agricultural and rural sector development

1.2.1 Production

According to calculations of the EAA¹ for Latvia, gross agricultural production value in constant prices² increased by 5% compared to the previous period and was 515.1 mln. EUR³ in 2004. In nominal prices gross agricultural production value compared to the previous period increased by 21%. It was the highest indicator of ten last years. Share of crop and livestock production each comprise traditionally ~50%.

¹ Economic Accounts for Agriculture

² Prices of year 2000

³ 1 LVL=0,671 EUR (average exchange rate in 2004; source: CSB of Latvia)

Total area sown in year 2004 had a very slight increase up to 899,2 thsd. ha. Half of this area is allocated for grain production, which is quite stable. Latvia has come to full self-sufficiency level for grains produced for human consumption, and favourable conditions on EU grain market encouraging growth in grain exports have contributed to the grain and also rapeseed production development. Further growth of grain production volumes could be expected for feed grain under the conditions of livestock sector development.

The most rapid growing crop sector in Latvia is rapeseed sector. Rapeseed production is influenced mainly by the price in the world markets: having no basis for expectation of significant world market price decrease, the production potential of Latvian rape seed sector has unlimited market. This is evidenced by the increase of planted areas in 2004 about 2 times compared to year 2003, rapeseed production increased about 2.8 times, with further increase by 40 % in 2005. The developments in bio-energy production in Latvia provide extra potential for production increase.

Productivity growth in livestock sector helped to keep the production volumes in all livestock production activities, even while the animal numbers were decreasing, especially this trend is typical for dairy sector. However further structural changes in milk sector are anticipated, because milk volume sold to processors was only 478.1 thsd.t or 69% of milk quota.

Beef and pork production remains stable – decrease of production units is compensated by animal number growth in more commercially oriented farming units. While poultry production, the sector with highest concentration rate, annually grows, increasing by 15% in year 2004. Enhancing competitiveness is the major factor for further development of meat production sector due to unachieved self-sufficiency level for all kind of meat.

1.2.2 Prices

In year 2004 compared to year 2003 producer prices increased for the major part of agricultural products. Considerable price changes appear for some products as a result of the EU policy price implementation or diminishing price gap due to price convergence process.

Price changes for sugar beet were the most remarkable in crop sector and raised 1,6 times. As the prices for grain in Latvia before accession were close to the EU prices, 2004 grain prices were close to the same. Fruits and berries is a very aggregate position therefore very little apple yield could be the main factor affecting the average price for fruits and vegetables.

In livestock sector the major rise of producer price was for milk – by 35.2%, beef – by 25.6% and pork – by 11,9%.

1.2.3 Agricultural Trade

Assessing changes in agricultural trade after Latvia joined EU, there must be mentioned more rapid increase in volume of exports in 2004 (34%) comparing with increase of imports (20%). Exports to EU countries increased even more – by nearly 50%. Looking to the balance of external trade, exceed of imports over exports in 2004 increased by 10,5%, (2003 it was 11%).

Latvian agricultural exports in last years mainly comprises of non-alcoholic and alcoholic beverages, processed fishery products, dairy products.

There is observed stable tendency for Latvian export flows to increase in share of EU countries – in 2002 volume of exports to those countries increased by 25%, in 2003 by 18%, in 2004 by 48%. In overall structure of agricultural exports EU25 countries took 59% in 2003, and 65% in 2004. The most crucial increase was observed in trade with new member states – by 65% in 2003, and share of those countries comprises 40%.

Assessing structure of Latvian agricultural imports, there remains tendency of prevailing products in import flow, which are not produced in Latvia at all or are produced with shortage

comparing with necessities for full coverage of consumption. Those include: alcoholic beverages, meat products, exotic fruits, vegetables (in winter period), vegetable oil, coffee, and tea.

The most important increase in imports comparing years 2004 and 2003 there was observed in following product categories: tobacco production by 57% or 10,3 million Lats, alcoholic beverages by 66% or 7,6 million Lats, pork by 34% or 4,3 million Lats, cocoa products by 33% or 4 million Lats, animal food by 23% or 2,6 million Lats.

Assessing Latvian agricultural import flows regarding trade partner countries there is heavy dominance of EU countries – 83 – 85% of imports are originating from those countries. In period of three years (2002 – 2004) there is observed increase of imports only from EU countries, volume of imports from another countries remains stable.

1.3 Agricultural and rural policy developments

The EU CAP 1st pillar policy measures in Latvia in years 2004 and 2005 were implemented within the frame of SAP scheme. The EU direct support was complemented from national budget until the maximum allowed level in the form of payments coupled to agricultural production in order to make agricultural support policy more similar to pre-accession conditions and to provide a gradual shift to mostly decoupled direct payments anticipated in near future under reformed SP scheme.

There is already decided on national level to continue SAP scheme at least in 2006. Different policy reform scenarios, which have been analysed within the frame of CAP reform impact evaluation have initiated public discussions about CAP reform full-scale implementation issues in Latvia. In order to get advantage for further development of agricultural sector through diminishing the gap in DP rates between Latvia and old EU member states caused by *phasing-in rule*, SAP scheme should be continued until year 2009 considering the opportunity to channel more financial resources for CNDP in SAP scheme compared to alternative SP scheme.

85% of direct support available within the frame of the EU CMO was paid to applicants (Table 1-1). Concerning definite coupled payments - in 2005 entire eligible area for SAP is expected to be declared. While, the payment application level for suckler cows and ewes premiums in 2004 was accordingly 14% and 54% only, because of little number of eligible animals, and there could be expected a future impact of payment availability on development of livestock sector.

Table 1-1 The EU CMO direct support available and granted in Latvia for year 2004

	Direct support,% of the EU-15 level	Direct support available, EUR	Direct support granted, EUR	Direct support granted/available, %
SAP	25%	30 480 000	26 424 996	87%
CNDP (coupled to production)	45%	55 067 362	46 170 583	84%
Total	70%	85 547 362	72 595 579	85%

Source: Ministry of Agriculture of Latvia, Rural Support Service, LSIAE calculations

The EU CAP 2nd pillar policy measures regarding rural development support in years 2004 and 2005 were implemented according to Rural Development Plan for Latvia. Total funding available was 123.4 mio EUR and 71% was paid to applicants. The biggest share of total support – 54% was available for LFA territories, and at the same were applications were received only 62% of the resources available in 2004. Available support is expected to become an incentive payment for renewing the farming activities also in LFA, partially limited prior the EU accession land.

Demand for *risk management* measures in agricultural sector has become as a topical policy issue in years 2004 and 2005 due with emphases on farmers training in risk diminishing. Insurance system held by public authorities would share the risk of farmers considering their risk preventive actions, private funding, and education. State policy compensatory measures should be implemented only to support risk preventive actions.

2 Assessment and Outlook

2.1 Wine sector

Non-significant sector for Latvia – there is no wine production in country. Latvia is importing wine for consumption, as well small amount of imported wines are filled in bottles and exported as sparkling wines.

2.1.1 Wine consumption

There is no reliable direct statistical data about wine consumption in Latvia. Consumption data can be derived from import – export data. Approximate calculated amount for year 2003 is about 15,4 liters of wine per person per annum.

2.1.2 Wine imports and exports

Year	Imports		Exports	
	milj. Lats	t	milj. Lats	t
2003	27,2	41742,7	2,4	5916,7
2004	29,4	n.d.	14,7	n.d.
2005	38,3	n.d.	29,8	n.d.

2.2 Sugar sector

2.2.1 Sugar consumption

Since 2000 there has been observed rapid growth in total sugar consumption in Latvia. In recent 5 years by steady increase of the purchasing power of population in Latvia, both aggregate demand and aggregate supply have been increased considerably and have provoked sugar consumption growth by more than a half from 2000 till 2004. Considering the decrease in number of inhabitants in Latvia, the growth of sugar consumption per capita actually has been growing more rapidly. From year 2000 till 2004 it has been increased almost by 60 percent. The annual growth of sugar consumption is gradually decreasing that affords ground for expectations of sugar consumption stabilization in a long-term. However, in recent 5 years annual amounts of sugar consumption (in dry state) have been steady and have varied about 19.5 kg per capita.

Due to lack of statistical information about structure of sugar consumption it is assumed that gross human consumption reaches 100% of total sugar consumption in Latvia.

2.2.2 Sugar import

By increase of effective demand and restricted diversity of domestic supply of food products since 2000 there have been observed the significant growth in import of food products in Latvia. Considering that since 2000 the quota system operates in sugar sector in Latvia and

actually defines volumes of sugar production, the amounts of import of sugar and sugar-containing products have increased rapidly in recent five years. From 2000 till 2004 sugar import in white sugar equivalent has increased by 70 percent, i.e. from 18 till 31 thousand tonnes. The import of sugar in dry state has been growing more rapidly and from 2000 till 2004 has increased threefold from 2.4 till 7.0 thousand tonnes. By the increase in sugar price the amount of sugar import in terms of money has been growing fivefold.

In recent 5 years all of the 10 main trading partners which imported about 90% of total sugar import in Latvia are from EU25 countries. But if in 1999-2001 more than 60% of sugar import in Latvia had been from Poland, Finland, Germany, Denmark and Lithuania. In 2002-2004 by growth in sugar price the major trading partners have been changed – less sugar have been imported from Poland, Germany and Denmark and more from Lithuania, Netherlands, UK and France. Therefore in 2004 the major trading partners have become Lithuania, Finland, Netherlands, UK and France.

2.2.3 Sugar beet area

Considering that sugar is produced only from local sugar beets without using a raw sugar the quota system has stabilised sugar beet branch in Latvia. Therefore from 2000 till 2004 sugar beet area has varied about 14 thousand ha, that is approximately 1.5% of total arable area, and has allowed to ensure stable income for sugar beet growers.

The location of sugar production points has the most important influence on the territorial location of area used for sugar beet production. Therefore more than 90% of total sugar beet area is concentrated in the southern regions of Latvia where both sugar factories are located.

2.2.4 Structure of production

In 2004 there have been 480 sugar beet growing farms in Latvia. Generally, holdings with sugar beets are larger than average in terms of both area and economic indicators. In 2004 the overall agricultural area for holdings with sugar beets (230,ha, of which 27.3 have been dedicated for sugar beet) has been larger than the average for all farms (22 ha). The overall economical size for holdings growing sugar beets has been 27.7 ESU, of which 12 ESU has been formed directly by sugar beet production. In 2004 96% of total sugar beet area has been located in the market oriented farms with economical size exceed 8 ESU. 50% of total sugar beet area has been concentrated in the 30 biggest sugar beet growing farms with an economical size more than 100 ESU.

Since 2000 when sugar company “AS Jēkabpils cukurfabrika” has become insolvent, there has been left 2 sugar factories in Latvia. In case of EU sugar CMO guiding principles, sugar producing quotas and sugar prices remaining unchanged, the quantitative development of sugar and sugar beet sector is going to be limited. The reform of EU sugar policy assumes that the major part of small EU sugar factories either should be closed or should change its type of activity after implementation of the reform. Considering that both of Latvian sugar factories are among the smallest sugar factories in EU there is no ground for expectations of sugar producers’ growth in Latvia. Owing to small number of sugar companies in Latvia the information about the main investors in sugar sector is confidential.

2.2.5 Yields

Considering that sugar is produced only from local sugar beets without using a raw sugar the quota system has stabilised sugar beet branch in Latvia. Total annual yields of local sugar beet have ensured 100% degree of self-sufficiency for sugar beet. From 2000 till 2004 sugar beet area has varied about 14 thousand ha, sugar beet yield per hectare has varied about 36 t/ha, but sugar yield per hectare has varied about 4.9 t/ha. In 2004 the sugar yield per hectare in Latvia was the 3rd lowest in EU and almost 2 times lower than in EU in general.

2.2.6 Sugar and isoglucose production

Since quota system operates in sugar sector in Latvia, sugar producers generally have ensured fulfilment of sugar quota. In 2000-2004 sugar production has varied about total (A and B) quota amount ensuring about 100% degree of self-sufficiency for sugar in dry state. Considering significant growth of food products consumption containing sugar, degree of self-sufficiency for sugar in white sugar equivalent has decreased up to 76%. In 2004 volume of sugar production per capita has been 28.65 kg which is one of the lowest indicators in EU. For example, in 2004 sugar production per capita has been 76.8 kg in Denmark, 41.45 kg in Germany and 42.75 kg in Sweden.

2.2.7 Production cost and competitiveness

Owing to small number of sugar companies in Latvia the information about production costs and competitiveness of the sugar sector is confidential.

2.2.8 Exports

Due to relatively high price level of home produced sugar, Latvia doesn't have continuous trade partners and respectively could not be identified as sugar exporting country in a wide sense. In 2000-2004 the annual variations of sugar exports have been based on single deliveries to the certain countries. For example, in 2000 89% of sugar export or 10.5 thousand tonnes has been exported to Uzbekistan, in 2003 94% of sugar export or 16.3 thousand tonnes has been exported to Tajikistan, Moldova and Ukraine, but in 2004 95% of sugar export or 13.9 has been exported to the UK and Lithuania.

Since quota system operates in sugar sector of Latvia, sugar beet growers, concerned about quantitative development of sugar beet branch in future, have been looking for sugar beet export potentialities. In 2003 4.9% of total sugar beet yield or 24.8 thousand tonnes has been exported to Belarus. In 2004 1.3% of total sugar beet yield or 6.8 thousand tonnes has been exported to German, Estonia, Lithuania and Ireland.

2.2.9 Policy issues

Since 2000 quota system has operated in Latvia and has determined volumes of sugar (as well as sugar beet) production. In 2004 the amount of sugar production quota A was 66400 tonnes and quota B – 105 tonnes. Implementation of sugar quota has had an important impact both on sugar beet producers and processors. So, on the base of sugar beet delivery contracts, sugar

beet producers has planned their activity in this commodity branch for a long term period by implementing modern sugar beet growing technologies, which demanded significant capital investments. On the ground of granted production quotas, sugar companies have made numerous capital investments in order to modernize sugar factories accordingly EU requirements. Accordingly to Regulation 1782/2003 from 2004 there has been applied Single Area Payment (SAP) scheme that apprehends direct payments to sugar beet growers only in SAP form (in 2004 – 20.66 EUR/ha; in 2005 – 26.44 EUR/ha).

Overall Latvia, as well as the most part of new EU member states, could have important disadvantages compared to EU-15 in the case of of sugar sector reform implementation results. The existing intervention mechanisms, which anticipates fixed intervention price, so far has guaranteed stable sugar beet price and has had to be taken into account by all involved producers. After the implementation of private storage mechanism for the smallest sugar producers in EU, which is the case for both of Latvian sugar factories, it could be much more difficult to realize sugar in the market. Sugar price cut endangers the existence of sugar sector in Latvia at all.

Annexes

Annex 1 Dynamics of some general economic and agricultural indicators in Latvia

	2003	2004	2005 1st half (p)*
GDP at current prices, mln.LVL	6318	7333	3977
GDP growth (at constant prices, %)	7.5	8.3	9.5
GDP per capita (Euro, current prices)	4212	4725	2457
Consumer price changes (%), as average per period	2.9	6.2	6.6
Average share of jobseekers in the total economically active population (%)	10.6	10.4	9.6
Foreign trade balance (% of GDP)	-21.2	-22.6	-20.0
Average interest rates in lats (short term and with a floating rate, %)	5.4	7.5	5.9 **
Average net wages and salaries, LVL/month	138	150	168
Changes in gross value added in agriculture:			
- at constant prices	-1.4	4.2	5.6
- at current prices	5.9	32.5	11.6
Agricultural income in % of average wages in total economy (per 1 employer)	42	74	...

* % values are shown of corresponding period of previous year.

** 2nd quarter.

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Annex 2 Crop and livestock production, sown areas and number of livestock in Latvia, 2000.-2004.

	2000	2001	2002	2003	2004	2004/ 2003, %
Crop production						
Sown area, thsds. ha						
Total,	881.1	869.8	887.7	851.1	899.2	105.7
of which						
- cereals	420.0	443.7	415.0	428.5	436.7	101.9
- rape	6.9	8.4	18.4	25.9	54.3	209.3
- sugarbeets	12.7	14.1	15.9	14.4	13.8	96.1
- potatoes	51.3	55.1	53.6	54.6	48.9	89.6
Production, thsds. t						
- cereals	923.6	924.0	1028.5	932.4	1059.5	113.6
- rape	10.0	13.0	32.7	37.4	103.6	277.1
- sugarbeets	407.7	491.2	622.3	532.4	505.6	95.0
- potatoes	747.1	615.3	768.4	739.0	628.4	85.0
Livestock production						
Number of livestock, thsds.(at the end of year)						
- dairy cows	204.5	209.1	204.6	186.3	186.2	99.9
- other cattle	162.2	176.0	183.4	192.3	184.9	96.2
- pigs	393.5	428.7	453.2	444.4	435.7	98.0
- poultry	3104.6	3621.0	3882.0	4002.6	4049.5	101.2
Production, thsds. t						
- milk	825.0	848.0	813.7	785.7	786.4	100.1
- meat, total (slaughter weight)	61.7	60.3	63.3	71.1	73.2	103.0
- beef and veal (slaughter weight)	22.4	19.1	16.0	21.12	21.6	102.2
- pork (slaughter weight)	31.5	31.6	35.9	36.9	36.8	99.7
- poultry (slaughter weight)	7.2	8.9	10.6	12.4	14.3	115.1
- eggs, mln.pieces	437.1	452.5	508.6	508.8	527.4	103.7
Average milk yield per cow, kg	3898	4055	3958	4261	4251	99.8

Source: CSB collection of statistical data 201, 2003, 2004 "Agricultural farms of Latvia"

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Annex 3 Producer prices of agricultural products in Latvia 2000.-2004., LVL/t

	2000	2001	2002	2003	2004	2004./2003.,%
Crop production						
Wheat	59.6	57.6	59.5	65.3	65.3	100
Rye	55.1	52.4	55.7	59.6	59.1	99
Barley	59.1	53.5	53.8	56.9	59.2	104
Oats	56.0	52.9	51.8	52.7	55.7	106
Rapeseed	102.3	121.8	121.4	135.5	127.1	94
Sugar beets	20.8	19.3	19.4	17.8	28.3	160
Potatoes	30.0	58.7	57.8	48.4	50.1	103
Vegetables	78	51.7	88.9	85.9	85.1	99
Vegetables in covered areas	355.6	321	338.4	370.6	369.1	100
Fruits and berries	113.3	126.5	97.8	140.0	320.4	229
Livestock production						
Milk	83.9	93.6	92.2	94.0	127.1	135
Beef*	334.9	438.6	406.8	300.0	376.9	126
Pork*	721.2	813.5	640.2	638.5	714.5	112
Poultry*	599.3	629.8	439.0	544.7	564.7	104
Eggs	39.8	40.7	32.8	37.1	37.8	102

Source: EAA for Latvia, CSB; * – live weight

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Annex 4. Data for Sugar sector

		1999	2000	2001	2002	2003	2004	2005
Sugar Beet								
Year								
Total Area	000 ha	15,5	12,7	14,1	15,9	14,4	13,8	13,5
Yield	tonnes/ha	29,2	32,1	34,9	39,1	37,0	36,7	38,5
Production	000 t	451,5	407,7	491,2	622,3	532,4	505,6	519,9
Processed	000 t	452,0	394,3	449,8	540,1	490,8	478,6	493,2
Feed	000 t	0,0	20,5	33,4	53,1	3,0	0,9	0,9
Sugar								
Production	000 t	66,5	62,8	56,0	76,9	74,9	67,1	n.d.
Imports	000 t	2,4	4,0	4,4	5,6	9,1	7,4	13,7
Exports	000 t	0,0	11,9	0,1	0,4	17,9	14,6	24,4
Consumption	000 t	65,0	54,4	59,0	60,1	63,7	68,2	n.d.
Value of Trade								
Imports	mlj LVL	0,4	0,7	1,0	1,2	1,8	2,6	6,2
	mlj EUR	0,7	1,3	1,8	2,1	2,8	3,9	8,8
Exports	mlj LVL	0,0	1,8	0,0	0,1	2,2	5,2	9,8
	mlj EUR	0,0	3,1	0,1	0,2	3,5	7,7	13,9
Balance of Trade	mlj LVL	-0,4	1,0	-1,0	-1,1	0,4	2,6	3,6
	mlj EUR	-0,6	1,8	-1,7	-1,9	0,7	3,9	5,1