

THE GOVERNMENT'S ROLE IN DETERMINING PRICES, TAXES AND CREDITS FOR INDIVIDUAL FARMS

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1 General characteristics of individual farms

In Latvia land is being returned to its users. Within the framework of land reform by May 1st in 1992, there were already 41.3 thousand individual farms with total acreage 620 thousand ha. This comprises 14% of agricultural lands. The average size of an individual farm is 15 ha.

Individual farms gradually start to specialize in one type of farming. Two thirds of farms specialize in crop production, which requires less farm inputs and labour inputs. Only one third of farms want to specialize in cattlebreeding. In 1991 there were in average 4 head of cattle, 3 milk cows, 5 hogs and 3 sheep per farm.

The total yield from individual farms in 1991 was 7 thousand tons of milk, 1 thousand tons of meat (live weight) and 6 million eggs. It is respectively 4.2%, 3.3% and 0.6% of total farm products.

The unsatisfactory situation as to the material and technical resources is an obstacle to a more rapid development of agriculture. There are only about 33% of tractors and 20% of other agricultural machinery needed in individual farms. Thus by May 1st in 1992 there was 1 tractor per 17 ha of agricultural land in individual farms. This figure does not describe the actual state of each individual farm, because the distribution of machinery is uneven. To reinforce the material and technical basis is a prime agents for further development of individual farms.

2 The role of prices in the development of individual farms

By the end of 1991 the Council of Ministers of the Republic adopted a resolution on liberalization of prices on all types of agricultural products. The objectives of the price liberalization were to establish the necessary prerequisites for further development of production with the regard to all types of agricultural producers, including individual farmers, as well as to equalize the income brackets of agricultural producers with those of workers employed in other branches of national economy. As the fixed producer prices of agricultural products considerably lagged behind the rate of price increase for industrial goods, the gap between the incomes of people working in these two separate branches widened.

However, it should be noted that the liberalization of prices in all branches of national economy still does not mean a transfer to market economy in the classical sense of the word, because the issues of privatization of land and real estate have not been solved yet, and the state monopoly on basic production means still exists.

At present the farmer has the right to participate in the procedure of determining the producer price for his products. The prices of milk and meat are being set as a result of negotiations and also agreement between the producers of agricultural products, processing enterprises and traders.

At the same time state guaranteed minimum purchase prices, which were set for the main agricultural products: crops 1000 roubles per ton, sugar-beet 250 roubles per ton; flax straw 2100 roubles per ton, milk 1050 roubles per ton, beef cattle 7300 roubles per ton (live weight), hogs 7600 roubles per ton (live weight).

Yet, the government has set a margin for profit relation to charges for the processing enterprises - the same for dairy factories and meat processing plants - it should not exceed 15%. The traders profit rate has also been restricted, so that it should not exceed 25% for bread, 20% for dairy products, and 15% for meat, meat products.

The pricing system of this type enabled the agricultural producers to defend their interests. There was a steep rise of producer prices and on March 1st in 1992 they exceeded average prices of 1991 7 times for milk, 4 times for beef and 6 times for pork.

At the same time the results of indexation for the first quarter of 1991 indicated that production costs in agriculture have increased during this period averagely by 10.8 times, however, profits have increased only by 7 times.

Agricultural producers suffer from lack of money for production development, and the volumes of production are confirming to decrease. If during the first quarter of 1991 the total product of cattlebreeding and poultry farming comprised 85% of that of the same period in 1990 and in dairy farming 82%, then the results for the first quarter in 1992 were 78% and 80% respectively.

In order to protect the producers of agricultural products under the circumstances of inflation, recommendations were handed in to revise the state - guaranteed purchase prices. From March 6th in 1992 the state - guaranteed purchase prices were revised, and they were set close to the actual prices which existed at that moment.

During the first three months of price reform the prices for agricultural products were not restricted by anybody: it was the producer who set them, especially in the areas where the Farmers' Centre had a strong influence. Now due to limited market both at home and abroad, the big processing plants try to stick to the state - guaranteed purchase prices. However, the prices for material and technical resources raise continuity.

Thus, by May 1st in 1992 the price increase for electricity was 25 fold, for diesel fuel 46 fold, for fertilizers 24-93 fold, for agricultural machinery 10-20 fold if compared to 1991.

The forecast for this year as to the increase of production costs is 31 billion roubles or 7.2 times more in comparison with the last year. This means that the state - guaranteed purchase prices for the main types of agricultural products ought to be increased by 1.5 to 2 times. The result will be an inevitable rise of retail prices for foodstuffs.

By May 1st (compared with december of the last year), the retail prices had increased 2.3 times for milk, 3 times for beef and pork. It should be noticed that after the revision of the state - guaranteed purchase prices, the producers' prices and the wholesale prices

set by the processing enterprises became stable. The retail prices continued to grow. For example, in May they had increased by 1.2 times for milk and dairy products and by 1.14 times for beef and its products, if compared with March.

A new price increase for agricultural products began with June 1st in 1992, when the government lifted the restrictions on profits for processing enterprises and restrictions of turnover tax for traders.

With the view of the present situation of wages compared to the consumer prices, the purchasing power of the population has dropped considerably. A decrease in sales volumes testifies to the fact. Thus, during the first quarter of 1992 (compared with the respective period in 1991) the consumption of foodstuffs has decreased by 53% for dairy products, by 44% for meat and meat products, by 31% for bread and bread products.

During this period the retail prices have increased 2.5 times, but the wages have increased 2 times for industrial workers and only 1.6 times for agricultural workers. In order to bring closer the income level of agricultural workers to that of working in other branches of national economy, arrangements for price stabilization should be made, which would be impossible without state subsidies.

3 The regulation of individual farmers' income

If we compare agricultural production with other branches of production, its main features are a slow turnover of assets and seasonality. This means that producers' prices cannot be the sole source of income for agricultural producers. The income of agricultural producers should be regulated:

- by state - guaranteed purchase prices
- by tax exemptions
- by subsidies.

Especially the new individual farms who have just started farming need help, because they have money shortages for construction and they have to purchase material and technical resources.

3.1 Credits

Consequently a resolution was adopted in January of 1992 with regard to the condition for allotting credits to individual farmers from the state budget and to the terms of repayment. The annual interest rate for long-term credits envisaged for the purchase of agricultural machinery, buildings, for expansions or purchase of residential houses and production buildings as well as for buying cattle, has been set up to 7 per cent for individual farmers, and 12 per cent in average for all the rest entrepreneurs.

The resolution envisages also to draw money from the state budget in order to give a discount for the long-term credits for 50%, if the farmer has used them timely and purposefully.

The critical situation which has set in as to granting long-term credits for individual farmers might seriously detain the process of privatization and the agrarian reform. The individual farmers' demand for long-term credits 12 billion roubles in 1992.

The government has found possibility to grant only 25% of the sum needed by farmers by now. This means that a special stabilization fund for farmers should be founded. It should be built of:

- subsidies from state budget
- state and local government non-budget fund for privatization
- the money from commercial banks, companies and international finance institutions
- contributions made by individuals

3.2 Subsidies

In order to achieve a balance between the income of agricultural producers and solvent demand of population, it would be useful to subsidize the price increase for material and technical resources. This would promote the reduction of production costs. Producer should be subsidized in the process of purchasing material resources. Subsidies should be based on standards for resource expenditure per 1 ha of agricultural lands and the amount of land used. Taking into consideration the vital importance of crop farming, the subsidies could also be differentiated according to the amount of crops sold.

Subsidies for material resources will help to stabilize conditions for agricultural production and will restrict the steep rise of prices for agricultural products.

The subsidy policy should be closely linked with tax policy. This will make it possible to evaluate correctly the production conditions for each region and to state the income level of agricultural producers. Simultaneously a mechanism for collecting different rent from the producers who work under better conditions can be introduced. It should also be mentioned that the present tax policy is not flexible enough as to the economic conditions of individual farms, including soil fertility and favourable geographical position.

Taking in consideration the above said, it is almost sure, that many areas in Latgale and Vidzeme would not be able to compete with those in Zemgale and Riga district, where the cost of products is considerably lower. The farmers in the former areas will be forced to leave their farms because they will have gone bankrupt. As a result of this there exists a danger to lose agricultural lands in great amounts. It has already happened in the recent past when due to an unsuccessful agricultural policy about 1 million ha of agricultural lands have been lost. It would be simply inadmissible in the present situation when our market is suffering from shortages. If developing individual farms is our objective, subsidies should be allotted to the individual farmers, who are under the worst farming conditions.

Conclusion:

- Government should support the establishing and developing individual farms by setting low interest rate on credits, determining small taxes, and by subsidizing the farms with bad farming conditions,
- the agricultural workers are expecting the Supreme Council of the Republic to adopt the law on privatization of processing enterprises. The law will promote the establishing of branch societies (for dairy processors, for sugar producers, etc.), where the farmer becomes the owner of processing enterprises and is interested in the final product.

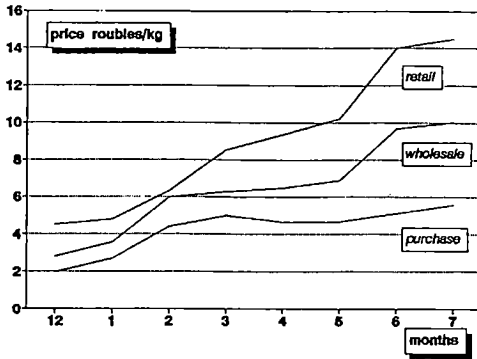


Figure 1. Dynamics of average price of milk in 1991-92.

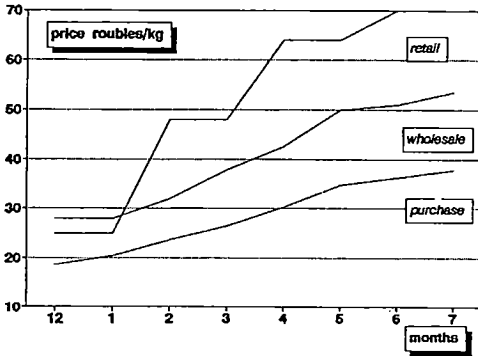


Figure 2. Dynamics of average price of beef in 1991-92.

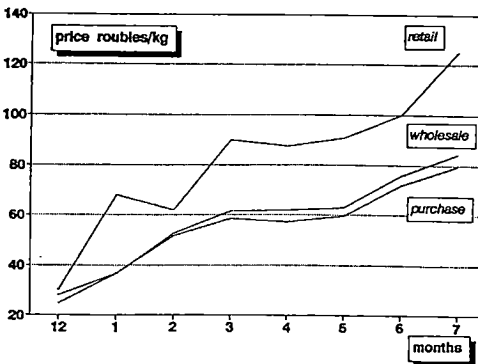


Figure 3. Dynamics of average price of pork in 1991-92.