

## FINANCE AND CREDIT

### Experience and Provisional Impact of Direct Support Payments in Latvia

*Dr.oec. Irina PILVERE,*

Rural Support Service, [Irina.Pilvere@lad.gov.lv](mailto:Irina.Pilvere@lad.gov.lv),

*Mag.oec. Andis RUKMANIS,*

Rural Support Service, [Andis.Rukmanis@lad.gov.lv](mailto:Andis.Rukmanis@lad.gov.lv)

#### **Abstract**

The article represents results of research on state support payments and EU direct payments interaction and synergy in the years 2003 and 2004, as a result of which amount of financial support significantly changes and its impact on the regions in Latvia may also change.

Article shows calculations and results of analysis at the level of territories of nine regions of the Rural Support Service between the level of utilized agriculture area and amount of agricultural products produced by farmers, and received amount of financial support, in comparison to the total state and EU direct payments available in Latvia after accession to the EU.

More detailed analysis has been made to assess general situation in Latvia, as the amount of support dynamically increases and in 2005 it exceeds the amount received in 2003 by 4,3 times and that in 2000 many times. It has been found that after accession to the EU, support amount for each ha of utilized agriculture area in regions of Latvia is equalizing, but it increases in the regions with low intensity of agricultural production.

**Key words:** State support, EU direct payments, Single Area Payment, Complementary National Direct Payments.

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#### **Introduction**

After accession to the EU, for Latvia as well as for other new Member States, the types of support, conditions, as well as support priorities and amounts paid out in subsidies in agricultural sector significantly changes [8]. The term 'EU direct support' comprises different types of payments, such as single area payment (SAP), complementary national direct payments for agricultural crops, livestock, milk quota, seeds, support for potato starch growers, producer organizations etc.[3,4,5]

Increasingly significant share in the farmers' incomes is coming from support measures of the Rural Development Plan, such as support for less favorable areas and other agro environmental measures, support for semi-subsistence farms, support for meeting EU standards, etc.

Until accession to the EU, in Latvia as it is known, only national state support was available

which was foreseen by Agriculture and rural development law at the level of 2.5% from the state basic budget expenditure and EU pre-accession support for agriculture and rural development (SAPARD). After accession to the EU the types and sources of financial support for agriculture have expanded and opened up not only different direct payments, but also RDP measures and support from two structural funds, as well as, specific state support measures.

In total these measures increased available funding by 4,3 times. This fast and radical change in the opportunities of farmers and rural areas requires specific research on the effectiveness of the support.

Those considerations also determined the main aim of the article - to analyze whether and how EU direct payments have changed amount of support and its impact on agriculture development within regions of Latvia.

Within the scope of this aim, the following tasks are solved:

- to compare the levels of direct support measures one year before accession with the first year after accession to the EU;

- to analyze and evaluate support levels in regions of Latvia in connection with utilized agriculture area and the amount of produced goods.

At the outset of this research, authors have developed main hypothesis: accession to the EU provides a variety of possibilities for farmers to receive support, but due to financial support of direct payments the intensity of received support and as a result the impact of the support at the level of regions is changing.

### Materials and methods

This research has been carried out on the basis of legal texts of the Republic of Latvia, data from the Central Statistical Bureau and EUROSTAT, Rural Support Service data, as well as the annual reports on agriculture issued by the Ministry of Agriculture and research materials about support programs and impact of direct payments on the agricultural products market [6,16,17]. Although direct area payments are very significant part of decoupled support framework of the Common Agricultural Policy of the EU, especially so in Latvia, their impact on production and market is not fully clear as the available data is scarce and with short history [6, 16].

Following methods have been applied to carry out this research: overall method of analysis, data grouping, dynamic time line analysis, descriptive statistics and logical constructive methods, the calculation of the correlation indicators, as well as experts' evaluations and opinions.

In order to perform the research, the following assumptions were adopted:

- the term 'EU direct support payments' encompasses all European Agricultural Guidance and Guarantee Fund (EAGGF) guarantee financed measures in 2004 [3,4,5 ];

- SAPARD and structural funds financed activities are not taken into account because their main objective is to promote structural changes in agriculture, fisheries, forestry and rural development mainly through investments;

- in using Rural Support Service operational information all data has been grouped at the level of nine regional agriculture departments of the RSS:

- Austrumlatgale regional agricultural department (RAD) – Rēzekne and Ludza districts;

- Dienvidlatgale RAD – Daugavpils, Krāslava and Jēkabpils districts;

- Viduslatvija RAD – Preiļi and Madona districts;

- Ziemeļaustrumi RAD – Gulbene, Balvi and Alūksne districts;

- Ziemeļvidzeme RAD – Valka, Valmiera, Cēsis and Limbaži districts;

- Lielrīga RAD – Aizkraukle, Ogre and Rīga districts;

- Zemgale RAD – Bauska, Dobele and Jelgava districts;

- Ziemeļkurzeme RAD – Talsi, Tukums and Ventpils districts;

- Dienvidkurzeme RAD – Liepāja, Kuldīga and Saldus districts;

- by using the data for 2003 of the Central Statistical Bureau of Latvia, produced goods has been expressed in the money value – in the case of grain according to established intervention price on 1st November 2005, for dairy and meat products according to Market & Price Review for October 2005 [1,11,14];

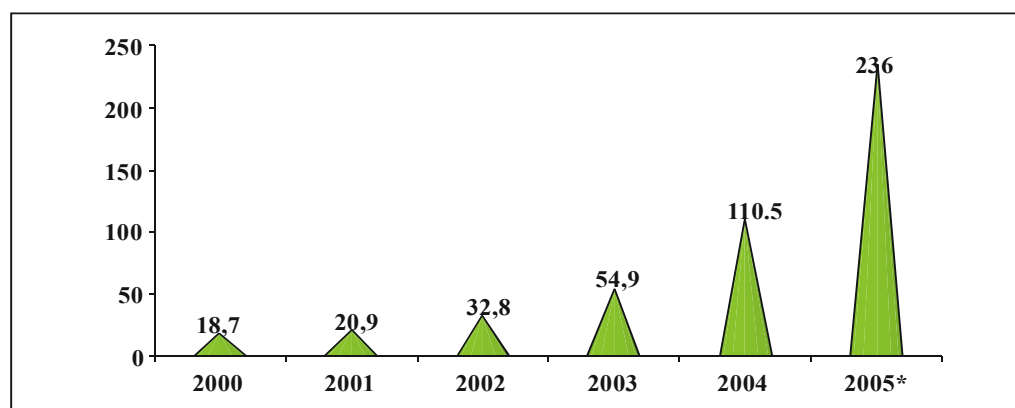
- RSS data on state and EU direct payments in the regions are used; nevertheless no data for year 2005 are taken into account, due to the fact that in the 9 months of 2005 only 44% of the year's estimated payments have been executed [15].

## Results

### 1. Aggregated support indicators and areas

State financial support policy for agriculture development in Latvia was started in 1994 with the allocation of national subsidies. Initially support was insignificant and fragmentary, but with the adoption of Agricultural law in 1996 a specific system was established and foreseen, that support amount can not be less than 3% from the annual basic budget expenditure [9]. Later in 2004 Article 5 point 3 of the adopted Agriculture and Rural Development law established that state support in subsidies can not be less than 2,5% from annual basic budgeted expenditure [10]. Since 2002 in addition to state subsidies, farmers in Latvia are receiving payments from projects carried out within the SAPARD program, but from the year 2004 different types of EU support are made available. The dynamics of total support amount from the year 2000 is presented in figure 1.

In total in the period from 2000 until the accession to the EU, the available support for farmers in



\*forecast

Source: RSS operational information [15]

Fig. 1 Total amount of support for agriculture and rural development in the period 2000 – 2006, in mill. LVL

Table 1  
Proportion of Latvia's regions of the total UAA, value of the agricultural produce and amount of support

Region	Share (%)			
	UAA	Value of products in 2004	Support payments in 2003	Support payments in 2004
Austrumlatgale	8,2	5,8	4,7	7,7
Dienvidkurzeme	13,9	15,3	14,4	12,3
Dienvidlatgale	13,1	11,2	10,4	14,4
Lielrīga	9,5	12,1	12,2	8,7
Viduslatvija	9	7,4	7,7	9,4
Zemgale	13,8	20,3	17,7	15
Ziemeļaustrumi	8,7	5,8	5,5	7,6
Ziemeļkurzeme	9,8	8,9	10,4	10,7
Ziemeļvidzeme	14	13,2	17	14,2
Total	100	100	100	100

Source: Authors' calculations from CSB and RSS data [1,11,14,15]

Latvia has tripled and it has reached 54,9 mill LVL, where 20,8 mill LVL was SAPARD financing. The turning point was 2004, when total support amount doubled in comparison to 2003, due to the available EU direct payments, Rural Development Plan payments and structural funds. From calculations it can be seen that in 2005 these payments could once more double and reach 236 mill LVL or be 4,3 times more the respective amount in 2003. This amount is composed by following:

- final payments to farmers for area applications of 2004 season (rules foresee to carry out payments for applications of the corresponding year from December 1st until April 30th next year);
- advance payments for area applications of 2005 season – 100% rate for single area payments (SAP), 80% - for Complementary National

Direct Payments, 100% for RDP Agro environmental measures;

- payments under RDP measures for the year 2005 – support for semi subsistence farms, support for meeting EU standards, etc;
- first payments under common market organization measures – support for producer groups, beekeeping national program etc;
- payments for market support measures.

## 2. Regional structure and proportionality of national and EU support payments

In order to evaluate the distribution of received financial support by regions, authors have chosen four indicators – utilized agriculture area, value of produced production and amount of received total support in 2003 and, in order to estimate the differences also in the year 2004.

All these calculations are summarized in Table 1.

From the results of these calculations following conclusions can be drawn:

- intensity of land utilization in regions is very different;
- share of production value in Zemgale is 1,5 times bigger than share of used land;
- share of production value substantially exceeds share of used land also in Dienvidkurzeme and Lielrīga regions;
- in total 37% of land is used in these three regions, but they produce almost a half (48%) of all agriculture production in Latvia;
- specifically ineffective land use can be observed in Ziemeļaustrumi and Austrumlatgale regions;
- the greatest share of support payments in 2004 in comparison with the products value, were received by farmers in Ziemeļkurzeme and Ziemeļvidzeme regions;
- low value of produced goods directly correlates with low share of support in Austrumlatgale, Viduslatvija and Ziemeļaustrumi regions;
- the regional distribution of support has changed substantially in line with significant increase in the total amount of support in 2004:
  - support for Zemgale region is significantly less than its value of produced goods;
  - notably lower support can be seen also for Dienvidkurzeme and Lielrīga regions;

- share of support in Dienvidlatgale, Ziemeļkurzeme and Viduslatvija regions is not only significantly higher than the share of produced goods value, but also share of utilized land area.

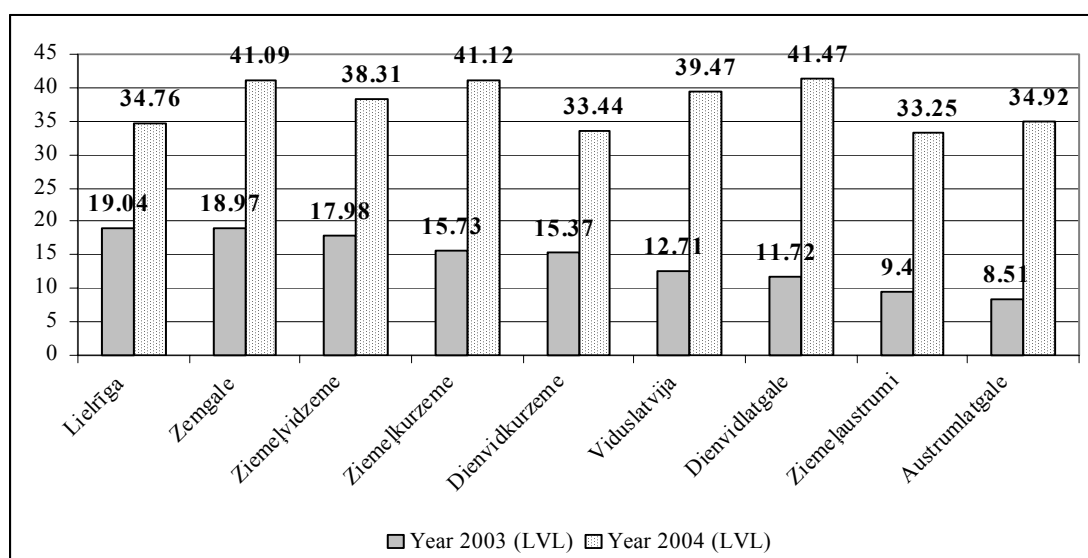
- in total support for agricultural production in less intensive regions exceeds the value of produced goods;
- by analyzing trends it can be concluded that allocated share of support for agricultural production decreases, but increases the amount of support for farmers, who produce little or even less of agricultural production.

In total the amount of support received in regions in 2003 was 27,2 mill LVL and in 2004 was 69,3 mill LVL, which is respectively 50% and 60% of the total support paid out in the country.

The absolute amount of support paid out per 1 ha of UAA is given in Figure 2.

This figure shows certain trends in 2003 and sharp changes in 2004. Analyzing trends of 2003 it can be concluded that:

- the greatest amount of support has been received by main commercial agricultural districts and regions – Zemgale, which gives largest share in crop production and Ziemeļvidzeme, where modern dairy production develops;
- Ziemeļaustrumi and Austrumlatgale regions with little number of farms but with absolute dominance of natural and semi subsistence farms have received twice less of support;



Source: authors' construction and calculations from RSS and CSB data [1,11,14,15]

Fig. 2 Amount of support per 1 ha of UAA in regions in 2003 and 2004 (LVL)

■ the aggregated amount of support per 1 ha is 14,82 LVL/ha, and it has fluctuated from 8,51 LVL/ha in Austrumlatgale up to 19,04 LVL/ha in Lielrīga, so the difference is almost 125%.

After accession to the EU, amount of support has increased on average by 2,5 times, reaching 37,76 LVL/ha and has substantially reduced the differences between highest and lowest rate of support:

■ the difference between the highest and the lowest rate of received support has decreased to 25%;

■ the largest amount has been received by farms in Dienvidlatgale, where support amount has risen 3,5 times;

■ the smallest increase in support has been seen by agricultural enterprises and farms in Lielrīga, Zemgale and Ziemeļvidzeme regions;

■ after accession to the EU the levelling of average rates of support between the regions of Latvia has taken place;

■ the greatest rise in support rate per 1 ha has been seen in Austrumlatgale – 4,1 times.

Further we have performed analysis using the grouping method of agricultural holdings, as a parameter using the area of agricultural land claimed for support.

From Table 2 it can be observed that almost one third of all support (~30,5%) was granted to natural or semi subsistence farms, where UAA is less than 20 ha. Small (50-99 ha) commercial

farms have received on average 3700 LVL each, which enables them to continue development. Large scale (more than 100 ha) agricultural enterprises have received in total 40% from the total support amount, or 27,7 mill LVL. Well planned utilization of this money creates a real base to increase their competitiveness.

The total amount of support allocated for farms, which cultivate area up to 200 ha, and which account for 99 % from the total number of farms, accounts for ~70% of all EU direct support.

### 3. Effectiveness of support in regions of Latvia

In order to measure potential and actual effectiveness of the support, we have chosen to use the correlation indicator between used support and obtained production (Figure 3). As can be seen, the situation is completely opposite to previously described correlation with UAA. Differences between support intensity per each production LVL among the regions in 2003 were insignificant – in Zemgale, where farmers produced the most value of production from each ha, amounting 206 LVL from each ha, support amount has been the same as in Austrumlatgale – 9 santimes per each 1 agriculture production LVL, but there the value of produced agricultural goods was only 98 LVL/ha. In Lielrīga, where they produce goods in the value of 180 LVL per 1 ha, farmers in 2003 received support of 10 santimes for each LVL of

Table 2

#### Structure of beneficiaries according to declared UAA and amount of direct payment support received in 2004 in Latvia

Submitted for support area groups (ha)	Support recipients within the group	Share from total number of support recipients	Received support in respective group (LVL)	Share from total amount of support (%)
0,3 – 9,99	40 320	60,29	10 456 494	15,31
10,0 – 19,99	14 891	22,27	10 318 292	15,11
20,0 – 29,99	4 699	7,03	5 801 913	8,50
30,0 – 39,99	2 014	3,01	3 548 755	5,20
40,0 – 49,99	1 191	1,78	2 748 948	4,03
50,0 – 99,99	2 095	3,13	7 747 865	11,35
100,0 – 199,99	948	1,42	7 191 644	10,53
200,0 – 499,99	485	0,73	8 496 621	12,44
500,0 and more	229	0,34	11 976 935	17,53
<b>Total</b>	<b>66 872</b>	<b>100,00</b>	<b>68 287 468</b>	<b>100,00</b>

Source: Authors' calculations from RSS data [15]

produced goods that is the same amount which was received by farmers in Viduslatvija, where the value of produced goods was only 117 LVL per 1 ha. Likewise, support amount in Dienvidkurzeme was 10 santimes, which was the same as for farmers in Ziemeļaustrumi and Dienvidlatgale, but the value of produced goods were respectively 1,7 and 1,3 times more.

Situation changes substantially in 2004, because the largest amount of support was received by regions, with the lowest level of produced goods from ha. In Viduslatvija, Dienvidlatgale, Ziemeļaustrumi and Austrumlatgale support was 0,34 – 0,36 LVL for each sold production LVL. In the highly intensive agricultural production regions – Zemgale, Lielrīga and Dienvidkurzeme the amount of support was only 0,19 – 0,22 LVL, or almost 2 times less.

#### 4. Discussion

Taking into account the calculations and data analysis presented in Figure 3, it is difficult to agree with authors Daina Saktiņa and William H.Meyers conclusion presented in the research paper „EU co-financed and national rural support programs in Latvia: in preparation for new programming period” that „in total it can be concluded that in the state created rural and agriculture sup-

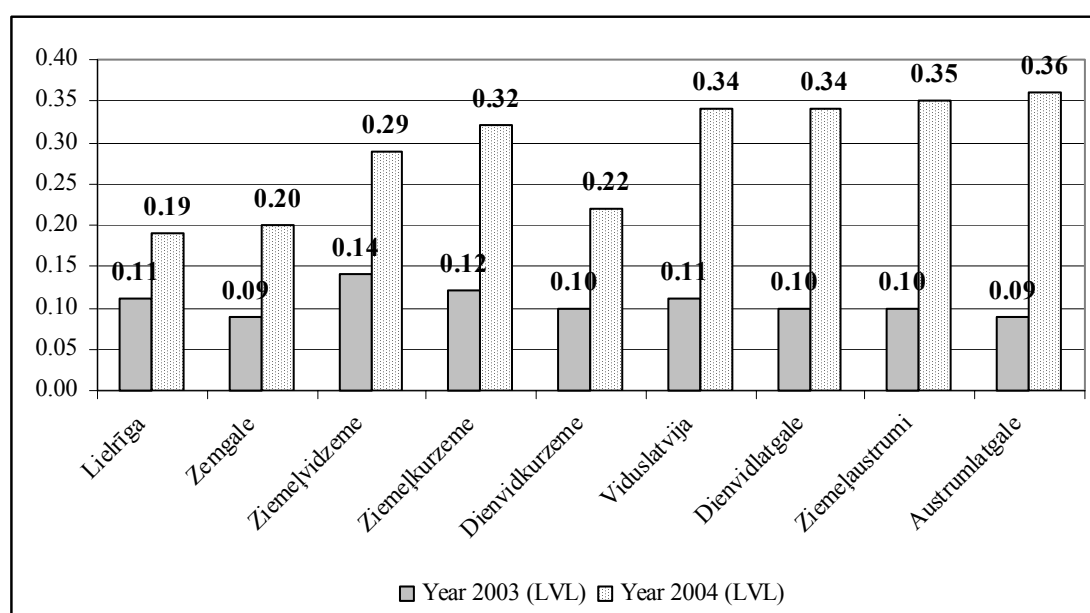
port policy, up to now the larger winners were farmers living and working in state’s central part and its bordering regions. As the policy uses very little differentiation of support rates and measures and, in general, the requirements to apply for support are similar for competitive enterprises and for the less successful companies, the amount of limited available support first of all, reaches more active and competitive entrepreneurs, who possibly, could develop their farm also without the help of support” [7].

Therefore in the situation when:

1. agriculture is only sector, where the amount of GDP decreased in 2003 [12];
2. productivity of employees in agriculture is very low [12,13];
3. calculating the added value for one employed person in agriculture, this was less than 10% of the average of EU Member States [13],

it is very important to balance out different support options – both national programs and state support, and EU payments, in order to effectively integrate needs and opportunities of agricultural production and rural development.

The new EU financial perspective for the period from 2007 to 2013 is approaching. The United Kingdom during its presidency in the beginning of November 2005 tried to resume negotiations



Source: authors' construction and calculations from RSS and CSB data [1, 11, 14, 15]

Fig. 3 Amount of disbursed support in LVL per 1 LVL of manufactured agricultural produce in 2003 and 2004

about the EU budget, but Member States still have different positions on the principles, which should be considered in order to agree the budget for the 2007 – 2013 period [2]. Besides, the delays in the budget approval might influence the implementation of support measures in the next period, because EU has agreed to reform the so called 2<sup>nd</sup> pillar or support for rural development of the Common Agricultural Policy (CAP). Besides, new Member States not later than by the year 2009, have to implement the reform of direct payments which was adopted in 2003, and which is implemented by old Member States already in 2005 and 2006. In these conditions it is important to balance out different types of support and to target them for the development of agriculture as sector, as well as for the comprehensive development of integrated rural economics and environment. Policy makers and also farmers should also consider first experience of EU direct payments, which comprise significant proportion of farmers' income.

## Conclusions

1. Total amount of support within last two years have significantly increased, however further increase will be slow and gradual, which will mainly depend from the budget priorities of the new financial perspective;

2. Amount of State support per 1 ha of UAA before accession to the EU substantially differed among regions – on average 2 times more of support was received by regions, with more intensive production of agriculture goods;

3. Amount of State support in the regions, calculating on the basis of produced agriculture goods before accession to the EU, was more equalized and differed on average by 20 – 25%;

4. Implementation of EAGGF support measures in Latvia reduces the differences among regions when estimating support amount for each ha of UAA, therefore current support level is not directly linked with the value and amount of produced goods;

5. After accession to the EU support intensity substantially increases in the regions, where farmers produce small amount of agriculture products, therefore support payments by in substance do not promote further development of agriculture sector, but could create directly opposite effect;

6. During the preparation of Rural Development Plan for the next programming period and selection of support measures, it would be necessary to evaluate also the experience of direct payments, in order to match the possibilities of further development of agricultural sector competitiveness and maintenance of rural environment and landscape.

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