CENTRE FOR CO-OPERATION WITH THE ECONOMIES IN TRANSITION

Review of Agricultural Policies

LATVIA

ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

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- to contribute to sound economic expansion in Member as well as non-member countries in the process of economic development; and
- to contribute to the expansion of world trade on a multilateral, non-discriminatory basis in accordance with international obligations.

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THE CENTRE FOR CO-OPERATION WITH THE ECONOMIES IN TRANSITION

The Centre for Co-operation with the European Economies in Transition (CCEET) was created in March 1990, as the focal point for co-operation between the OECD and the countries of Central and Eastern Europe. In 1991, the activities of the Centre were expanded to include the New Independent States of the Former Soviet Union and, the following year, Mongolia. In 1993, the Centre was renamed Centre for Co-operation with the Economies in Transition (CCET) to reflect its wider geographic coverage. Since 1991, the Centre has operated a ''Partners in Transition'' Programme for the purpose of providing targeted assistance to the countries more advanced in introducing market-oriented reforms and which desire to become Members of OECD. The ''Partners'' are now Poland and the Slovak Republic.

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During the period following World War II, Latvia was transformed from a primarily agricultural to an industrial economy. As a result, the population shifted from rural to urban areas, and, by the end of 1994, 70 per cent of the population lived in urban areas (one third being in Riga). The creation of large-scale industry was used to tie Latvia economically to the rest of the USSR. Large enterprises in Latvia, which depended on other Soviet republics for inputs, exported final products to the entire Soviet Union.

On 4 May 1990, the Supreme Council of the Latvian Soviet Socialist Republic formally declared the restoration of Latvian independence, re-establishing the Republic of Latvia. Most of the basic legal structures required for a market economy and a democratic political system have been put in place since 1990.

Latvia has achieved a certain degree of macroeconomic stability following the successful adjustment programme introduced in 1993. Economic recovery however remains limited for a number of reasons, including difficulties in the banking sector, the size of the shadow economy and the slow pace of structural reform. Following the sharp falls in real GDP in 1992 and 1993 (by 35 and 14.7 per cent respectively), the State Statistics Committee reported an increase of 0.6 per cent in 1994, but in 1995 GDP contracted once again, falling by 1.5 per cent. The high rate of inflation continues to be a cause for concern. After levelling out in 1993, a rate of 26.3 per cent was recorded in 1994. Rapid growth in the money supply – fuelled by capital inflows from abroad and higher import duties and tax rates (mainly on food products) – have been the main factors behind the rise in prices. Since February 1994, a fixed exchange rate policy has been pursued, and the national currency has been fully convertible for current and capital account operations. As the country's Central Bank has continued to focus on exchange rate stability, its support for a largely fixed exchange rate leaves the money supply highly vulnerable to capital inflows.

The privatisation process has proceeded slowly, except in agriculture and to some extent the food industry. Large-scale voucher privatisation began only in February 1995, and its pace was slow in 1995. The official unemployment rate increased steadily from 2.3 per cent at the end of 1992 to 6.4 per cent in mid-1994, and has more or less stabilised since then, with some seasonal variations. However, there is thought to be a relatively high rate of hidden unemployment in unprivatised industry and rural areas.

Due to the high level of shadow economic activity and the slower-than-expected recovery in GDP growth, the government budget deficit increased in 1994 and especially in 1995, when it is estimated to have reached 4 per cent of GDP. The government's increasing reliance on bank loans to finance the deficit has limited the credit available in the banking sector for business investment.

B. Agriculture in the overall transition

The livestock sector was developed with the objective of supplying Russia and other Soviet republics with meat and dairy products. Its high level of production was very dependent on input supplies from all Union funds. The political and economic reforms were accompanied by a sharp fall in agricultural production between 1990 and 1994. Compared to gross agricultural output in the last five years of the Soviet period, output in 1994 was down by 50 per cent, the decline being more marked for livestock production (60.5 per cent) than for crop production (37.8 per cent).

Notwithstanding these developments, agriculture remains an important sector in the Latvian economy. Indeed, between 1990 and 1992, agriculture's share of GDP increased from 10.3 to 12.4 per cent, largely as a result of the even faster rates of contraction experienced in the non-agricultural sectors (e.g., manufacturing and construction) of the economy. As output bottomed out in these sectors, while it continued to decline in agriculture, the latter's share of GDP declined to 8.5 per cent in 1994 and 1995. The privatisation and restructuring of agriculture led to increased employment in the sector. The share of agriculture in total employment increased from 13 per cent in the pre-reform period to 17 per cent in 1994 and remained at that level in 1995. In the transition period, agriculture became something of a safety net and an insurance against unemployment rather than a sector from which inefficiently used labour flowed to other activities.

In the reform period, the sector underwent a severe price-cost squeeze. Since the deregulation of prices in 1991, the prices of industrial inputs have increased to near world levels and have risen much faster than the prices of agricultural products. As a result, the terms of trade have deteriorated significantly for agricultural producers. In overall terms, beef, milk and grain prices are still below world market levels; only pig and poultry prices are close to world prices. The level of national income still remains very low compared to OECD countries and is a real barrier to growth in demand for agro-food products.

Even after the general liberalisation of prices, the government maintained certain price controls for agricultural products based on a "cost plus" pricing policy, in which changes in production costs were reflected in farm gate prices regulated by the state. The government set minimum prices and obliged state-owned food processing enterprises to apply them. That policy was abandoned for most products in 1993. Since then, only grains and sugar beet prices have continued to be controlled. Moreover, as the privatisation process in the food processing sector was completed, the government was no longer able to apply its minimum prices through state-owned enterprises.

Between 1991, when price liberalisation started, and the middle of 1994, consumer prices for all products rose relentlessly for three main reasons: higher input prices, especially for energy; processing enterprises attempting to compensate for the low utilisation of their production capacities by price increases; and government policies both of setting high prices for farm products (e.g., grains and sugar beet) and increasing border protection for agro-food imports. Changes in food consumption patterns were mostly driven by shifting relative prices, which led consumers to switch from dearer to cheaper products in 1991 and 1992. The main effect was a drop in the consumption of animal products. Despite falls in the consumption of the most expensive products, the share of food (excluding tobacco and beverages) in total household expenditure increased sharply in the transition period – from 29.4 per cent in 1990 to 48.2 per cent in 1992. From 1993 to 1995, however, the proportion fell back a little to 41.5 per cent in 1995, although that is still a very high figure by OECD standards. This not only limits consumption of non-food products but is also an obstacle to economic development.

C. International trade

1. *Agro-food trade*

In the past, Latvia was an important source of meat and dairy products for Russia and other NIS. Agro-food exports accounted for over 25 per cent of total estimated Latvian ''exports'' at the end of the eighties. From 1990 to 1994, these exports declined sharply, and in 1994 Latvia became a net importer of meat and dairy products. Figures for agro-food trade in 1995 indicated some recovery in exports relative to imports, resulting in a swing back to a surplus of US$28 million. This suggests that the agro-food trade deficit may have been only a temporary phenomenon, arising from the short-term dislocation of production due to the restructuring of the agricultural sector.

The geographical composition of Latvian agro-food trade shows different patterns for imports and exports. On the export side, Latvia's main markets remain the former socialist countries, which absorbed more than 80 per cent of its total exports in 1994, with the NIS accounting for the bulk (75 per cent). Exports to the CEECs (including the other two Baltic states) declined from 20 per cent of the total in 1993 to only 9.4 per cent in 1995. The share of exports to OECD countries remains low (11.5 per cent in 1995). On the import side, the OECD's share is much higher (47 per cent in 1993 and 63 per cent in 1995), with European OECD countries accounting for most of that. Imports from the CEECs and the NIS are lower and their share decreased in 1993-95 (that of the CEECs from 17.3 to 14.4 per cent and that of the NIS from 25 to 8 per cent).

2. *Trade relations*

Latvia's declaration of independence, the introduction of its own local currency and, finally, the collapse of the Soviet Union broke the former close economic ties between Latvia and the rest of the Soviet Union. Trade co-operation with central and eastern

European countries collapsed following the dissolution of the CMEA in 1990, and new trading relationships were established with these countries. New arrangements have also been worked out with the EU in the framework of a free trade agreement. Moreover, WTO accession terms are being negotiated in accordance with the results of the Uruguay Round of GATT negotiations.

Latvia started developing bilateral trade links by signing free trade agreements with the Scandinavian countries and Switzerland. These agreements do not cover the main agricultural products, only highly processed food. Trade concessions for specific agricultural and fish products are subject to quotas and these concessions are laid down in annexes to the main agreements that are signed and ratified separately. Since January 1995, Latvia's trade relations with Sweden and Finland have become subject to its agreements with the EU. In December 1995, a new free trade agreement with the remaining EFTA countries was signed, which replaced the existing bilateral agreements. These agreements also provide for agro-food trade to be governed by separate bilateral arrangements.

The free trade agreement signed with the Baltic states came into force in April 1994, but initially it did not include agro-food trade. A free trade agreement concerning agricultural products was signed by the Baltic countries only on June 16, 1996. Latvia has started discussions with the CEFTA countries and preparations are being made to sign bilateral free trade agreements with them. So far, Latvia has not applied officially for CEFTA membership because one of the conditions of membership is that it become a member of the WTO, which is not yet the case. Latvia is currently negotiating possible early membership of the WTO and as such would be bound by the provisions of the GATT Uruguay Round agreement relating to market access, domestic support and export subsidisation. It is proposing to bind a higher than current trade protection under WTO provisions, and it also wants to retain the option of granting moderate export support for agricultural products. At the end of 1995, Latvia's proposals were still under discussion and had not been accepted by other WTO members.

3. *Latvia and the European Union*

In January 1995, the trade regulations laid down in the free trade agreement with the EU came into force. This agreement gives Latvia access to the EU market on preferential terms and conditions. Latvian exporters of agro-food products were granted, in the first year a 40 per cent and in following years a 60 per cent reduction in EU tariffs within a system of quotas (increasing over time) for products such as pork, poultry-meat, some types of processed meat and several dairy products. Moreover, Latvia wants to negotiate an increase in the preferential tariff reduction to 80 per cent, the same rate as the EU has granted to the CEECs. Latvia also made reciprocal trade concessions to the EU. An Association Agreement between the European Union and the three Baltic Republics was concluded on 9 June 1995. The Association Agreement, once ratified, will take over the trade concessions of the free trade agreement. It gives Latvia the status of an associated country with the EU and envisages its full membership. However, this agreement can be expected to have only a limited effect on Latvian trade in agro-food products in the short term. Latvian exporters are having trouble filling their quotas because of poor quality and hygiene standards and their lack of marketing skills. However the agreement is important in a longer term perspective as it is expected to attract more investors to Latvia. With exposure to European standards, laws and trade practices, the agreement is also expected to help the modernisation of the Latvian economy.

Following the declaration made by EU heads of government in Madrid in December 1995, the earliest at which even the most economically advanced central and eastern European countries can hope to become members of the EU is the year 2000. Latvia will have to consider what policy to pursue in the meantime, given that it is unlikely to accede to the Union before the middle of the next decade. A gradual alignment of Latvian agricultural policy to current levels of EU support is ruled out by economic considerations and the probable commitments it will have to make to become a member of the WTO. Pending its possible membership of the EU, the best strategy for Latvia would probably be to maintain or create an open trade regime and a low price support policy in order to sustain and encourage greater competitiveness. This would be the best way to prepare the country to deal with whatever future scenario emerges, either within or outside the EU. Placing greater emphasis on improving the economic efficiency of the whole agro-food chain would enhance its competitiveness and improve the terms of trade for agricultural producers.

D. Agro-food restructuring

The essential components of agro-food restructuring were restitution and privatisation. Privatisation is the transfer of ownership of state or collective property to private hands and is distinct from the process of restitution, by which state or collective property also changes hands but reverts to those with a historical claim to ownership. The process in agriculture consisted of land reform and the privatisation of non-land assets of the formerly collective and state farms and agricultural services. In the food processing sector, the method of privatisation was a mix of asset distribution and sale of assets for shares or cash.

1. *Property restitution*

As part of the restoration of an independent Latvian Republic, Latvia declared the inviolability of ownership and property rights, providing a legal basis and legally requiring the restoration of property rights to former owners whose property had been seized under Soviet rule. Hence, the idea of restitution of property, or compensation when the actual property could not be returned, formed the basis of Latvia's renewed claim to national sovereignty and independence. As early as 1990, the Latvian Supreme Soviet decided that former owners or their heirs were entitled to restitution of, or compensation for, all property taken during the Soviet regime. A series of parliamentary laws governing restitution was subsequently passed; they provided for all claims for restitution to be made by 1 July 1994 and gave Latvian citizens living outside the country the right to apply for restitution.

2. *Land reform*

Land reform was designed to create a new structure of rural land tenure based on private property rights. It provided for the restitution of land titles to former owners and the free of charge allocation of land to Latvian residents intending to farm. The legislation had two simultaneous goals: the maintenance of land use and agricultural production, and the progressive establishment of a new land ownership structure.

Land reform effectively started in June 1990, after the ''Resolution on Agrarian Reform'' was adopted by the Supreme Soviet of the Republic of Latvia. The basic principles of land reform were subsequently enshrined in the ''Law on Land Reform in the Rural Territories of the Republic of Latvia'' passed on 21 November 1990. This legislation set up a network of land commissions at the national, regional and *pagasts* levels to manage land distribution. The reform was designed to reverse the Soviet nationalisation of land, so that all state-owned agricultural land, whether then used by collective farms, state farms, household plots, or any other Soviet-era entity, was due in principle to be reassigned to entitled users (restituted) and the remaining land privatised.

Former owners and their heirs, current occupants of the land, and persons who wished to receive land and were not employed in agriculture could all apply for a parcel of land. The acreage of land returned to private ownership was not restricted, but the restitution of more than 100 hectares required the approval of the Cabinet. Thirty-six per cent of all claimants were former landowners or their heirs asking for restitution of their land. Twenty-nine per cent of claims for land restitution came from urban residents, while two per cent came from persons living outside Latvia. Some 77 thousand individual farmers, including those that had already wished to begin operations in 1992, applied for a total of 1.8 million hectares of land for allocation by 1996. Around 100 thousand applications were received for 616 thousand hectares of land for part-time farms and an equal number for 240 thousand hectares for household plots.

Top priority went to claims from former owners or their heirs. After all requests for land restitution were granted or denied, the remaining land was to be allocated, in order of priority, to: expanding existing individual full-time farms; expanding individual part-time farms; the construction of a single-family residence; or to other individuals for any legally permitted use. Thus, any approved individual application for land, whether for restitution to previous owners or for a new individual farm, had a higher priority than continuing use of the land by a collective or state farm. This favoured individual farms at the expense of the former, large-scale farms. However, the law also stipulated that even approved claimants for restitution could be asked to wait up to five years (until 1996) if the land they claimed was needed by a corporate successor of a collective or state farm for its operation. At the end of 1995, the share of land retained by corporate farms (direct successors of the former co-operatives or state farms) was estimated at less than 5 per cent of total agricultural land, since only about 130 of these farms were still operational.

Land reform favoured the creation of individual farms. The five-year delay before the claimant could take over from the existing user was a temporary relief to the direct successors of the former collective or state farms. Since the delay expires in 1996, it is not yet clear how the remaining corporate farms will be affected. This question is especially valid as the law on the privatisation of non-land assets, which encouraged the transformation of these corporate farms during the reform period, was amended in 1995 to give the remaining farms the possibility of retaining their non-land assets and thus remain in operation. Present legislation is not clear as to whether a private farmer who receives land for farming as an individual (i.e., with a higher priority) has the right to create a new corporate farm together with other individual farmers. Once land reform is completed, the legislation should not specify the type of farming to be practised, but should leave it to the new owners of the land and non-land assets to decide what mode to adopt. This would at least seem to be in the interests of a more efficient and competitive farm sector.

The process of registration of land titles of new owners is taking a long time. Land Title Register offices only started to operate on 1 April 1993, and the first land titles were not registered until 31 May 1993. The registration process is likely to take a long time yet, which may also slow further restructuring of the farming sector, since only legally owned land can be mortgaged and freely traded.

3. Privatisation of collective and state farms' non-land assets

The legislation governing the privatisation of state and collective farms' non-land assets came into effect on 1 July 1991. It stipulated that the assets of collective and state farms in Latvia were to be privatised and that this form of organisation was to be legally liquidated at the end of the process. Property shares were used in the privatisation of these farms. Two criteria determined the proportion of the total share value of the corporate farm to which each recipient was entitled. Firstly, some shares were given as compensation for non-land assets seized during collectivisation. Secondly, other shares, but no less than half of the total equity, were allotted to former farmworkers in proportion to their contribution to the farm during its operation. In practice, most farms assigned about one-third of their total property share value as compensation. The property inventory, which had to be approved by a general meeting, had considerable influence on the privatisation of property, as it listed lots to be privatised. These lots were indivisible for the purposes of privatisation and were a determining factor in the structure of the farms that emerged. After the general meeting of shareholders had approved the corporate rules (by-laws), the share list and the property inventory, the collective or state farm was then reorganised into a new legal entity, such as a joint stock, shareholding, or limited liability company.

Once legally organised, the new corporate farm could begin to distribute non-land assets. Any shareholder had the right to claim for any lot or lots from the inventory, at the price indicated on the property list, paying for it with cash or shares. If other requests to buy the lot were received, the item was sold for shares at a closed auction to the highest bidder. Once all lots from the inventory were purchased the corporation was liquidated.

This procedure proved to be quite efficient in liquidating the corporate farms that were the successors of the former co-operative and state farms. To protect the remaining corporate farms, an amendment was voted in May 1995 allowing these corporate farms to retain non-land assets needed for their further existence. The amendment seems to conflict with the aims of the original legislation, which was clearly designed to encourage the sale of corporate farms' non-land assets to private individuals or groups of individuals. But as mentioned previously, this measure is now preserving the non-land assets used by these corporate farms, although their right to hold on to the land they are operating against the claims of individuals expires in early 1997. The situation of remaining corporate farms is thus unclear.

4. *Emerging farm structure*

The restructuring and privatisation of agriculture has led to fundamental changes in farming in Latvia. From the original number of more than 600 corporate farms established on the basis of former collective and state farms (operating in 1991 on 92 per cent of total agricultural land), only 120 or 130 were in operation at the beginning of 1996. The other corporate farms were liquidated during the process of privatisation, once all their non-land assets had been sold to private individuals. During privatisation, other corporate farms were established by individuals using privatised assets. On 1 January 1995, some 464 new corporate farms were operating. Altogether, corporate farms – both newly created ones and the successors of collective and state farms – were operating on 17 per cent of all agricultural land in 1995. As a result of the structural adjustment of Latvian agriculture, therefore, large-scale farms now account for a small proportion of total agriculture production.

Individual farms are now the cornerstone of Latvian agriculture, operating on 80 per cent of total agricultural land. The individual farming sector includes two different groups of producers: *i)* family farms, which are supposed to be full time and to generate their income from production for the market; and *ii)* part-time farms and private subsidiary plots, where agricultural production is a complementary source of income, since output is earmarked for family consumption on the farm rather than for the market. In 1995, some 64 000 family farms averaging 20 hectares in size occupied 47 per cent of total agricultural land. Part-time farms and private subsidiary plots accounted for 32 per cent of agricultural land. Although it is difficult to make a clear distinction between farms producing for the market and those engaged in self-subsistence farming, in the present situation some 40 per cent of agricultural land is probably operated by farms that are not producing for the market but are dependent on non-farming sources of income.

The primary privatisation process is almost completed and further changes in farm structure and type of farming will depend on decisions taken by the new owners of land and non-land assets. New farm structures will continue to undergo adjustments both for individual and corporate farms. A neutral policy aimed towards the different forms and types of form and structure would seem at this stage the best possible policy approach.

5. *Privatisation of upstream and downstream industries*

With the exception of the agricultural machinery industry and one plant producing liquid fertiliser, Latvia had no industrial plants producing inputs for agriculture during the Soviet era. The privatisation of these large enterprises was subject to the same rules and legislative measures as other formerly state-owned industrial enterprises. As the privatisation process was very slow in this area, none of these enterprises had been privatised by the end of 1995. There were also many small production units, parts of large agro-service enterprises, specialised in the production of agricultural machinery. These plants were privatised under the same rules as other agro-service enterprises, and most were in private ownership by the end of 1995.

The privatisation of agricultural processing and agro-service enterprises in Latvia started in 1993. The law provided for each enterprise to be privatised individually under separate procedures. Privatisation projects were approved on a case-by-case basis by the Ministry of Agriculture or by a privatisation commission acting on the authority of the Ministry.

Agro-service enterprises were split into smaller independent entities and privatised with the participation of farmers' associations, which were offered about 50 per cent of the shares. Shares that were not sold to them, together with the remaining 50 per cent, were offered first to the employees of the enterprises and then to other individuals. From the original 122 enterprises, 871 units were created for privatisation. By 1 November 1995, 797 of them had been privatised and the remaining 73 (in general the larger ones) were in the process of being sold.

One of the main goals of privatisation was to integrate farming and food processing enterprises. Privatisation projects reserved a share of preferential shares for producers of the relevant agricultural product, grouped in co-operatives or producers' associations. For some sectors such as meat processing, bakeries or sugar plants, less than 50 per cent of the shares were offered to farmers (25 to 35 per cent in the case of meat processing, for example). For the grain processing industry, the law stipulated that the share must be at least 51 per cent, and on average about 60 per cent of shares were sold to farmers' co-operatives or associations. The greatest degree of integration between farmers and processing enterprises is to be found in the dairy sector. The smaller local dairies were given free of charge to the revived or newly established Dairy Farmers' Associations. The larger central dairies were privatised as joint stock companies and at least 70 per cent of their shares were allocated to the dairy producers' associations at 25 to 50 per cent of their nominal value.

The food processing sector was almost completely privatised by the end of 1995. The process was complete for the dairy and meat industry by November 1995, and almost so for bakeries and sugar plants. The privatisation of grain processing factories was less advanced, with only seven out of 17 sold off at the end of 1995. However the lack of financial resources and a lack of technical, marketing and business skills on the part of the farmers forming the farmers associations and processing co-operatives that are the main shareholders may hold back the development of the downstream industry, which is vital for the prosperity of agriculture. Extensive vertical integration, brought about by

LVL 20 per tonne (plus transport costs) was set for sugar beet by the Ministry of Agriculture and paid by the state-owned sugar plants.

c) Investment support

To support investments in agriculture, the government created several institutions between 1992 and 1995. Two specialised organisations were set up, but because of a general lack of domestic long-term credit resources and budgetary constraints, they were forced to rely on credits obtained from foreign governments and international organisations. Little preferential credit has been advanced to the agricultural sector and has been targeted mainly at the development of individual farming.

In 1994, more selective eligibility criteria for preferential credit were introduced, requiring an economic assessment of the projects concerned. The same year, the government decided that one of the two specialist institutions should shift its focus from providing support only for agriculture to a broader range of investment in support of the rural economy in general. Although the resources allocated to that programme are limited, it indicates that the government is targeting not just agriculture but the whole range of rural activities.

The Latvian State Mortgage and Land Bank was established in 1993 to provide medium- and long-term credits on mortgage contracts and to represent the state in land dealings within the framework of the land privatisation process. Because of the shortage of credit available and the delays in land registration (credit can be given only with the security of property registered in the Land and Real Estate Register), the creation of this new institution could not in itself resolve the credit problems of agriculture. Credits from this bank will become more important in the future, when farmers will be able to raise loans against property. Land mortgaging will help mobilise resources for investments in agriculture once land reform is completed, including the registration of land titles. The most efficient way to promote investment in agriculture would seem to be to use available resources to speed up the process of land registration.

d) Tax concessions

In Latvia's new tax system, agriculture is granted important tax concessions, providing significant indirect support to agriculture, especially to individual farmers. Income tax is not payable by individual farmers and enterprise profit tax was not applied to agriculture until 1995. Since 1995, only smaller enterprises have been exonerated from profit tax; other agricultural enterprises are granted a tax discount of LVL 10 per hectare of agricultural land.

Agriculture also pays a reduced rate of social tax (half the standard rate). Property tax is not payable on assets used for agricultural production. For individual farmers, a land tax exemption can be granted for a maximum of five years under specific conditions, such as farming in less favourable conditions and major investments to improve the land. Exemptions from the land tax are granted by the local government authorities which collect the tax.

e) Direct payments

Subsidies to agriculture were introduced in 1994 as part of the Law on the State Budget. The total amount in 1994 was LVL 6.6 million. Most of these funds (LVL 5 million) were used to support higher quality inputs (livestock breeding as well as high quality seeds) in the form of direct payments per hectare or per animal. Some of the funds were also used to support agriculture in special regions, such as flax production. However, of the budgeted amount of LVL 13.2 million, only LVL 5.5 million were disbursed in 1995 under these programmes.

4. Environment and rural development

Before 1988, conflicts of interest between production and environmental norms meant that the latter were often neglected. Although Latvian agriculture undoubtedly contributes in a positive way to the quality of the environment, the negative environmental impacts are more obvious. The most important negative externalities of agricultural production are groundwater contamination through the use of fertilisers and pesticides and local pollution caused by the high concentration of livestock production, leading to problems with organic fertiliser disposal. With the increase in chemical input prices and the worsened terms of trade for agriculture, the use of these inputs declined having a positive influence on the environment.

Problems in enforcing environmental protection laws, and especially the former USSR regulations that are still in force, have become increasingly difficult as land and inland waters are returned to former owners and development pressures arise between environmental institutions and the reinstated landowners. In 1995, the Ministry of Environmental Protection and Regional Development of Latvia drew up a National Environmental Policy for the next 20 to 25 years. It is to be written into the National Environmental Policy Plan and the National Environmental Action Programme, which have still to be adopted by the Cabinet and approved by parliament (*Saeima*). One of the primary objectives of this policy is to reduce contamination of food by nitrates, pesticides, heavy metals, radionuclides resulting from incorrect and excessive use of mineral fertiliser, organic fertiliser, pesticides and other agro-chemicals. If policy objectives are to be achieved, there is a need for a clearer identification of priorities and in particular of the regulatory and economic instruments to be employed.

A rural development policy is at a very early stage of formulation but is still regarded as an aspect of regional policy. Under the Latvian rural development programme, substantial progress has been made in analysing the situation in rural areas, mainly at district (*pagast*) level, and in laying the foundations of a Latvian rural development policy. But the mechanism and criteria for its application still have to be defined, and funding to be found. An integrated rural development policy is of great importance for Latvia if it is to achieve a better balance between social and economic opportunities without distorting market signals or damaging its rural heritage.

When formulating a Rural Development Policy, it is important to consider agriculture as only one (albeit important) economic activity in rural areas. There is a general tendency for the economic importance of agriculture in the total rural economy to decline over the long term. To try solving the specific (social, environmental, income disparity) problems of rural areas solely through increased support to agricultural production would distort the market and would probably be one of the least efficient (most costly) ways of tackling them.

F. Assistance to agriculture

The level of support or assistance to agriculture is estimated by using the concept of Producer Subsidy Equivalents (PSE). The PSE measures the money value of transfers from consumers and taxpayers to the primary agricultural sector arising from all government policies affecting farmers' interests. Corresponding Consumer Subsidy Equivalents (CSEs) are also calculated. They estimate the tax paid by consumers because of the higher domestic prices maintained by market price support.

Total support to Latvian agriculture, as measured by the aggregate PSE, declined between 1986 and 1995. That period can be divided into two phases. In the Soviet era, support was high, averaging 80 per cent from 1986 to 1991. In the 1992-95 period, when the economic reform and transformation of agriculture were going ahead, support to Latvian agriculture was greatly reduced, with the PSE dropping from 79 per cent in 1991 to minus 82 per cent in 1992. But it increased again in the following years (i.e., lowering the implicit taxation of agriculture producers) and levelled off at a level of protection close to zero in 1994 and 1995.

Over the whole period, the most important component of total support, was Market Price Support (MPS). In the Soviet era, internal prices were isolated from world market prices and import competition by the centrally planned system of production and trade. In the case of dairy and beef, moreover, producers received additional support in the form of direct supplementary payments over and above the MPS. The switch to a market economy and free trade (and related exchange rate changes) resulted in a sharp decline in the MPS component and in total support to Latvian agriculture, as measured by the PSE.

In the Soviet period, the level of consumption subsidies was around 50 per cent of the market transfers from consumers; although CSEs were substantially lower than the PSEs, they nevertheless indicated transfers from consumers of around minus 39 per cent. Consumption subsidies remained quite stable over the period and variations in CSEs were due in the main to changes in the levels of market transfers resulting from variations in world market (reference) prices. In the first years of reform, consumer subsidies were cut sharply in 1991, while market transfers from consumers continued, resulting in very high negative percentage CSEs. In 1992, consumer subsidies were abolished completely, however because of the substantial devaluation of the currency, the CSE in 1992 showed a huge implicit market transfer to consumers, which mirrored the high implicit taxation of agricultural producers that year. As a result of a further reduction in market transfers in the following years, transfers to consumers declined in 1993 and 1994. In 1995, transfers to consumers increased slightly again, with the percentage CSE rising to 10 per cent.

In the Soviet period, support to livestock products dominated total support, accounting for more than 80 per cent of the total, which was partly due to the high share of livestock in agricultural output. However, there was less difference in net percentage PSEs than between livestock and crops. From 1986 to 1990, the degree of support measured as the percentage PSE averaged 81 per cent for livestock products and 77 per cent for crop products. In 1991, support for livestock products declined to 60 per cent but that for crop products rose to 106 per cent. In 1992 and 1993, there was a general decline in support, with producers being implicitly taxed; in general, the rate of taxation was higher for livestock products than for crops. In 1994 and 1995, the tendency reversed again, when positive transfers went to the livestock sector while crop products were increasingly taxed, mainly due to the increase in world reference prices. Increased border protection measures in 1994 also contributed to the increase in livestock PSEs in 1994 and 1995.

The decline in overall support to agriculture expressed in the PSE reflected the fundamental shift from a planned to a market-oriented economy and is consistent with the wider exposure of Latvian agriculture and the overall economy to world market realities. The fall in support to strongly negative levels in 1992 and 1993, indicating an implicit tax on agriculture, was a result of the overall changes in the macroeconomic environment, and of a certain transition inertia, rather than of any deliberate agricultural policy. Indeed, the implicit taxation, resulting largely from the devaluation of the local currency, was not specific to agriculture, since all other sectors were also facing similar transitional adjustment difficulties to these new macroeconomic conditions. The strongly undervalued local currency, especially in 1992 and 1993, was introduced as a macroeconomic measure to prevent a serious deterioration in the balance of payments (particularly the current account balance).[1] When trade was liberalised and the Lat made fully convertible, the effective undervaluation of the currency protected the economy, including agriculture, against excessive imports, but the negative effect was the increase in the prices of imported inputs such as energy, which caused inflationary pressures. On the other hand, it also enhanced (temporarily) Latvia's export competitiveness in foreign markets. This level of macroeconomic protection, not specific to agriculture, is reflected to some extent in the series of PSEs calculated at official and adjusted exchange rates. The discrepancy between the two sets of figures measuring the development of support to agriculture confirms that overall support to agriculture in the transition period, calculated at official exchange rates, was influenced more by macroeconomic developments and specific macroeconomic policy measures (including monetary policy) introduced during the transformation period than by the specific agriculture policy measures themselves. Any effects of agriculture policy measures were eroded by persistent macroeconomic instability and in particular the high level of inflation. The main conclusion to be drawn from this is that macroeconomic stabilisation and general economic recovery were more important for agriculture during the transition period than specific agricultural policy measures introduced in an unstable macroeconomic environment.

G. Conclusion

This study has assessed the progress made in the introduction of market reforms into the Latvian agro-food sector. On many counts, progress has been substantial, particularly in view of the challenges involved in moving from a command to a market-oriented economy. By the end of 1995, for example, the process of privatising and restructuring agriculture and the food industry had almost been completed in contrast with other sectors of the economy. Latvia has succeeded in establishing a strong individual farm sector, and a large part of its farming sector has the potential to very quickly become highly competitive and market oriented. Problems nevertheless remain in several areas. In land reform, the slow process of land registration is hampering the whole process of land privatisation and discouraging investment. The lack of business management skills among operators of individual farms, which now account for over 50 per cent of total agricultural land, and the high percentage of subsistence farming are factors that are hindering the development of a competitive agricultural sector.

The progress made by the Latvian government towards developing a market-orientated agricultural policy framework can be measured partly by the trend in the PSE. As in all other central and eastern European countries, support has fallen sharply. The decline in Latvia was mostly due to macroeconomic developments, especially the massive devaluation of the currency, and to an inefficient downstream sector that did not allow farmers to take advantage of higher border prices for agricultural products. The more inefficient the downstream sector, the longer this implicit taxation of agriculture will last. It would seem better for policy-makers to address these inefficiencies rather than to increase price support. The special preferences given in the privatisation of food processing industries to agricultural producers' associations, which lack capital, experience, marketing and management skills, are unlikely to contribute to such efficiency gains, which are essential for Latvia's agro-food sector.

Latvia has liberalised trade with the EU and some other European countries. To take advantage of the new trade opportunities thus opened, improvements must be made to standards and product quality in the agricultural sector. An agreement of free trade in agro-food products with the neighbouring Baltic states has yet to be negotiated. Membership of the WTO, which is a policy goal, will set limits on the level of support and protection Latvia can provide to agriculture. In the meantime, Latvia has succeeded in laying the foundations for a more market-oriented agro-food sector. The next steps should focus on introducing improvements to rural infrastructure and promoting greater competition along the whole agro-food chain.

Part II

PRIVATISATION AND RESTRUCTURING OF AGRICULTURE AND FOOD INDUSTRIES

A. Basic framework for the privatisation process

1. *Restitution*

The Soviet state nationalised almost all production assets and most physical property, including land, in Russia during the 1920s and did much the same thing in Latvia after annexing the country in 1940. Former owners lost their property without compensation, and newly created assets automatically became state property.

In 1990, after Latvia had regained its independence, the Latvian Supreme Soviet decided that former owners or their heirs should be entitled to restitution of, or compensation for, all property expropriated during the Soviet era. A series of legal acts governing restitution was subsequently adopted, which provided for all restitution claims to be made by 1 July 1994.

Effective privatisation of some state property began even before the USSR collapsed. The Soviet system frequently suffered from the fact that incumbents of particular state jobs, such as enterprise managers, were able to control state property for their own benefit, treating "state property" as though it were their own. The economic reforms introduced in the late 1980s, particularly the introduction of procedures for leasing assets to the "labour collective" (in practice the managers) with the subsequent right of purchase and legalisation of "co-operatives" (actually private enterprises), had the effect of amplifying that phenomenon, as managers transferred assets and revenues from their state-owned enterprises to the new "private" co-operatives they controlled.

Asset-stripping privatisation continued in Latvia after the principle of restitution was adopted and the first national laws on privatisation were passed in 1991. Individual ministries retained control over the privatisation of state assets until 1994, allowing officials to determine the recipients of the property. However, the privatisation process proceeded slowly up to 1994, partly because of the perceived unfairness of it.

Under 1991 legislation, the relevant ministries and municipalities were also responsible for privatising small and medium-sized retail and service companies. Purchasers of those businesses were not allowed to buy their buildings and land but instead were offered leases pending clarification of real estate property rights. The land and floor space of commercial facilities attached to buildings that included housing units were subject to the jurisdiction of the condominium authorities created as part of the separate process of housing privatisation that began only in the autumn of 1995.

In 1993, the *Saeima* instituted procedures for distributing privatisation vouchers to the population. Each person's voucher entitlement was based on his number of years' residence in Latvia, with a one-year voucher having a nominal value of LVL 28 (equivalent to the estimated cost of half a square meter of apartment). Every holder of a Latvian residence permit who lived in the country before 31 December 1992 was entitled to "year vouchers", one for each year of residence up to that date. In addition, every Latvian citizen was entitled to an additional allocation of 15 vouchers. Former political exiles and prisoners received extra vouchers in proportion to the time they had spent in exile or jail.

Individuals who successfully claimed the right to restitution of nationalised property but whose property could not be restored or who did not wish it restored in kind were also eligible for compensation vouchers under the voucher privatisation law. Compensation vouchers conferred certain special rights in privatisation sales: for example, until 1996 state land could only be purchased with compensation vouchers, while at auctions of the stock of enterprises being privatised compensation vouchers were worth twice as much as ordinary privatisation vouchers.

All eligible people were scheduled to receive their privatisation vouchers during 1995, with the exact date varying from place to place. Vouchers were distributed as a booklet naming the holder, summarising his length of residence and compensation voucher entitlements, and providing a place for authorised banks to certify the holder's voucher transactions.

The state-owned Latvijas Krajbanka (Savings Bank) and Sakaru Banka (The Post Bank) issued and registered further transactions in vouchers. The resale price per voucher ranged from LVL 0.5 to LVL 7 in 1993 and 1994.

The procedures for using vouchers to claim state property were not laid down until 1994, when the *Saeima* passed legislation creating the Latvian Privatisation Agency. That legislation called for most state property previously under the control of individual ministries to be transferred to the Privatisation Agency and for at least 50 per cent of the shares of enterprises being privatised to be sold for vouchers. Although after the settlement of restitution claims, all state property, including agricultural land, had to be privatised, the Latvian Privatisation Agency was not empowered to organise and manage the privatisation of agricultural land. Other agencies were set up to handle the privatisation of agricultural land and agro-food sector enterprises.

The Privatisation Agency divides the shares of an enterprise to be privatised into three parts. In general, at least 50 per cent of the shares plus one are sold for vouchers and cash to one bidder qualified in an auction. Ten to fifteen per cent of the shares are reserved for sale to the employees for vouchers and cash. The remainder is then offered to the public for vouchers. Requests to buy the publicly-offered shares are submitted to authorised banks, and their actual sale is handled by the Riga Stock Exchange, which reopened in July 1995.

As of June 1995, only about 1 per cent of all outstanding vouchers had been utilised. The sale of the 500 or so large enterprises that were transferred to the Latvian Privatisation Agency (LPA) for privatisation under the 1994 legislation began in February 1995. By October 1995, 374 enterprises had been selected for privatisation by the LPA and by the following month 300 of those privatisation projects had been approved.

2. *General rules and goals of agro-food privatisation*

In the summer of 1990, the Latvian Supreme Council adopted a resolution entitled "On agrarian reform", which set out the government's plans for reforming the whole agro-food sector. The resolution provided for the necessary procedures to be put in place for achieving three main goals:

- Land reform to create a new structure of rural land tenure based on private property rights. This generally provided for the restitution of land titles to former owners and the free allocation of land use for people currently working in agriculture and elsewhere. In fact, land reform legislation had two simultaneous objectives: the maintenance of land use and agricultural production and the progressive establishment of a new land ownership structure.
- Transition to a market-oriented agro-food sector to replace the former administered structure. Prices were to be freed throughout the sector. Property rights to non-land assets (buildings, machinery, livestock, supplies and unfinished goods) were to be clarified and individualised by distributing collective and state-farm property, and former owners and their heirs were to be compensated for non-land assets taken from them during collectivisation. Upstream and downstream industries were to be privatised and their monopoly powers abolished.
- Transformation of government agencies to support and regulate market relationships. The administrative organs, such as the old party committees and the Ministry of Agriculture, that had directed and run command agriculture were to be abolished or completely reorganised.

By formulating general policy goals in this way, the Supreme Council sought to cover all the main elements needed to dismantle the Soviet system of command agriculture and create a market-oriented sector. The resolution also clearly indicated that the final outcome of the process should be the complete break-up of the existing state and collective farms and their replacement by a different pattern of land tenure and farm organisation based on the individual farmstead system common in Latvia before 1940. The reforms were also intended to encourage entrepreneurship and the long-term modernisation of the sector, and thus ensure its profitability. Between 1991 and 1993 parliament passed at least a dozen major laws, to implement the various parts of this program.

To understand the changes in the ownership and organisation of farms and upstream and downstream enterprises since 1990, it is necessary to go back to the inter-war situation, since that was the explicit inspiration of the current reforms and was frequently cited as a policy precedent in the policy debates.

Because of the land reforms carried out in Latvia in the 1920s and 1930s, clear private property rights in agricultural land had been established by 1940. But following the USSR's annexation of Latvia that year, all land was nationalised without compensation. Between 1949 and 1950 farmers were compelled to transfer all non-land assets to collective ownership. In principle, every farmer was a part owner of all collective property, but in practice control over the assets passed to the state. The policy-makers responsible for the 1990s reforms set themselves two goals: to restore clear private land property rights through land reform and to ensure the equitable distribution of the non-land assets of collective and state farms to individual owners. Both processes provided for restitution of, or compensation for, land and other assets seized from private owners during the Soviet period.

3. *Historical background of current agricultural policy*

a) Agrarian reform in the 1920s and 1930s

Until the early 19th century, Latvian agriculture was manorial, with enserfed labour, generally ethnic Latvians, working for state-imposed landlords (often ethnic Germans). Following the abolition of serfdom in the Russian empire in the 1860s, increasing numbers of Latvians began to purchase their land from the landlords, establishing family farmsteads. By 1918, when Latvia gained its independence, there were a significant number of such "old farms" in the Latvian countryside.

Between 1920 and 1937, independent Latvia reformed its land ownership and exploitation system. Remaining manorial land (about half the country's total arable land) and state lands were redistributed. Minimum and maximum farm sizes were established by law. Farms that declared arable farming or animal husbandry to be their main activity had to have at least 10 hectares of land. After that reform, no agricultural land holding was allowed to exceed 50 hectares, except for a few "old farms" that were already larger than that. The newly-established farms averaged 22 hectares in size, while mergers resulting in farms of between 22 and 50 hectares required government approval. As a result, 85 per cent of all farms were owner-operated family enterprises by the mid-1930s (Table II.1).

Smaller farms, usually of five to six hectares, were part-time operations whose main sources of income were non-agricultural activities. Blacksmithing, carpentry, pottery, handicrafts or similar occupations were the main income sources of these farms, while their agricultural output tended to be directly consumed by the family rather than marketed. Land parcels of less than two hectares in rural areas and one hectare around towns were allowed as subsidiary plots on the land subject to reform.

In the 1920s, upstream and downstream agricultural enterprises were largely operated by small-scale private entrepreneurs or co-operatives. In the late 1930s, the state's influence over these enterprises grew. At the same time, powerful state-owned organisa-

Table II.1. **Number and size of farms in Latvia in 1935**

Farms classified by size in hectares	Number	%	Total area in hectares	%	Average in hectares
Up to 1	44 078	16.0	13 669	0.3	0.3
1-2	11 611	4.2	17 668	0.4	1.5
2-5	22 878	8.3	79 450	1.8	3.5
5-10	44 089	16.0	336 203	7.5	7.6
10-15	39 689	14.4	495 448	11.0	12.5
15-20	38 167	13.8	667 085	14.9	17.5
20-30	35 448	12.9	844 406	18.8	23.8
30-50	24 302	8.8	948 469	21.1	39.0
50-100	14 365	5.2	936 797	20.9	65.2
Over 100	1 071	0.4	147 769	3.3	138.0
Total	275 698	100.0	4 486 964	100.0	16.3

Source: Central Statistical Bureau of Latvia (CSBL).

tions exporting products such as butter and bacon were created. This state-dominated system is often referred to in contemporary policy debates.

b) The Soviet period

The Soviet regime nationalised all land on 22 July 1940, but farm operations remained private. The maximum individual size of farm was reduced to 30 hectares and the surplus land was redistributed by the state. The owners of small and medium-sized farms were left to work their land for a time. Following occupation by the German army in 1941, previous land use rights were restored, but property rights remained vested in the state. Restitution of property rights only started towards the end of German occupation. When Soviet forces reoccupied Latvia at the end of the war, Soviet laws nationalising land and limiting farms to 30 hectares were reintroduced. Collectivisation also started after the war, but the process was not supported by the farmers. The first collective farm (*kolkhoz*) in Latvia was established in 1946, but despite a major propaganda campaign, only 49 collective farms had been created by 1 January 1948. A year later, however, there were 893. Universal, enforced collectivisation began after 25 March 1949, when thousands of families were subsequently deported to Russia.

During the forced collectivisation, collective farms (*kolkhozy*) were created throughout Latvia. All farm families on the territory of the future collective farm had their land and productive assets expropriated without compensation. The collectivised assets were valued at prevailing prices, which were very low. That value was introduced in the accounts in two equal parts – half as a share fund and half as collective (not shared) fund. Theoretically, when the last member of a family left the kolkhoz, the person could receive the monetary value of the share. But such cases were very rare and that possibility existed only up to 1965. The government gave the new collective farm organisation the right to use the land, and could (and did) reassign land from one farm to another, or even to a non-agricultural land user. The new kolkhoz organisation became the owner of the collectivised non-land assets. In return, farm families got only the right to work on the collective and to maintain a small household plot. Wages were paid to the farm members out of "profits" from production (gross margin). Since the farms were subject to "voluntary" production plans and required to deliver their produce to state agencies, and since the prices paid by the state were generally kept low until at least the mid-1960s, collective farmers often received little (or even nothing) from the collective for their work.

In theory, the new collective farms were production co-operatives, and their highest authority was a periodic general meeting. But in practice the farm chairman, appointed after consultation with the Latvian Communist Party, ran the farm. "Members" had no choice about whether or not to join the kolkhoz, or which one to join. Anyone who left to work elsewhere could not receive back any part of what his family had "voluntarily" contributed to the farm.

The fields of the collective farms were worked in common, so that former individual farms' fields were reorganised and their old boundaries, as well as the sites of their old buildings, were often ploughed under. Inter-farm roads were laid to serve new, large-scale collective production facilities, and "social assets" such as stores, schools and services were also established and maintained by the farm to promote the new pattern of large-scale collective enterprise. Moreover, many of the old private farm buildings fell into ruin, as it was not permitted to repair buildings located outside villages.

The collective farms provided most of the services that local government or public utilities would supply in market economies. They were required to pay for the upkeep of roads on their territory and for the construction and operation of village utilities, services and social amenities, although items such as schoolteachers' or nurses' salaries might then be paid by the appropriate ministry. All these additional activities became part of the overall costs of agricultural production and had to be covered by agricultural prices or by a subsidy given to collective farms.

The collectives were generally administratively divided into smaller "brigades", to work a particular group of fields or operate a particular livestock facility. The first collective farms were fairly small, but then the Soviet regime decided to amalgamate small collectives into larger ones. In March 1950 Latvian farms began to combine, with the result that the number of *kolkhozy* in Latvia was reduced from 4 118 in May 1950 to 1 776 by 31 December 1950. The former collective farms often became organisational units within the new, larger farms.

By the early 1950s almost all agricultural land was organised into collective farms that averaged 300-500 hectares in size. Mergers to create ever larger farms continued in the following years (Table II.2). Units grew to an average size of 2 000-4 000 hectares by the early 1980s. One major purpose of the mergers was to incorporate weak farms into stronger, prosperous ones in the hope that the managerial expertise of the good farms would help pull up the bad ones. Often, of course, the performance of the enlarged farm actually declined, because it was unable either to maintain its facilities or to preserve its previous productivity.

Table II.2. **Number and size of farms, by 1 November 1955**

(numbers, thousand hectares)

Farm type	Number	Total area	Agricultural land	Arable land	Average area
Collective farms	1 394	3 494.3	2 565.5	1 669.4	2.510
State farms	37	230.6	158.2	115.2	6.232
Other agricultural farms	484	121.8	86.3	53.1	0.252
Agricultural farms – total	1 915	3 851.7	2 669.0	1 837.7	2.018

Source: Central Statistical Bureau of Latvia (CSBL).

Growth in farm size was accompanied by the enforced resettlement of the rural population from individual farmsteads to large villages. Facilities such as machinery storage and minor repair shops, fuel depots, and other supply agencies were initially organised separately from the farms in order to provide better control over farm operations. After 1959, the machine tractor stations were reorganised and merged with repair and service enterprises, but their machinery was sold to the collective farms. Such operations, however, continued to be centralised in the main farm villages, coming to serve larger and larger areas as the farms grew in size.

Individual production units within Latvia's collective farms also tended to grow over time. By 1989, there were more than 200 cowbarns large enough for more than 200 head of cattle and some two dozen pig feedlots capable of handling 10 000-30 000 animals. It was often difficult to ensure adequate supplies of feed to such large production units, animal diseases spread easily within them and they created major environmental problems.

Initially, the Soviet regime established almost exclusively collective farms in Latvia. In other parts of the USSR, state farms (sovkhozy), on which all production assets were state-owned and operated by state employees, had often been created during collectivisation. However, up to the 1950s they were generally created out of large manor farms or were new farming enterprises set up on previously idle lands. Since Latvia had broken up large land holdings in the 1920s and 1930s and had little unoccupied land, only a few state farms were created initially on the little idle land available.

The first state farms appeared in Latvia as early as 1941, created out of large "old farms", but their number was limited. A second period of state farm creation started in the early 1950s, when the least viable collective farms were transformed into state farms to keep them functioning. By converting weak collectives into state farms, the state became directly responsible for their wages and investment. State farms continued to be created in Latvia until the early 1980s. By then, the policy adopted by the Soviets in the late 1960s of providing all collective farmers with state-guaranteed wages and pensions had practically eliminated the differences between the two types of farm. In the 1980s, some of the weakest state farms were again reorganised, this time becoming "agricultural subsidiaries" of profitable state industrial plants. Unlike other former socialist countries of the Soviet bloc (e.g., the CEECs), the Soviet system organised large agricultural units within the major state industrial enterprises in Latvia essentially designed to provide food for their workers.

As was generally the case throughout the former Soviet Union, these processes tended to make even the remaining collective farms increasingly dependent on the state for financing and operational decisions, despite their theoretical independence and supposed collective ownership. This was deliberate and accorded with the tenets of communist political economy, which held that state or national ownership is the highest and most perfect form of ownership, whereas collective ownership should be considered only as a transitional form.

In the 1970s and 1980s, the state and collective farms also became an increasing burden on the state budget, as increasing amounts of capital investment failed to increase total production or enhance productivity to any great extent and probably benefited service and supply agencies more than the farms themselves.

Every household employed on a collective or state farm that worked a minimum number of days on the large farm had the right to keep a "household plot" (formally, a "personal subsidiary farm") for gardening and for keeping a small number of animals for its own use. Normally, they were allowed one or two cows, a few pigs, some poultry and a small plot of land, generally not more than half a hectare on kolkhozy and no more than 0.15 hectare on sovkhozy. Occasionally, the farm families might be allowed to use some land in the large farm fields that the collective or state farm was not working. These private plots produced much of the potatoes, vegetables, meat and milk available throughout the entire former Soviet Union. In 1990, Latvian private plots produced 62 per cent of all potatoes, 45 per cent of all vegetables, 27 per cent of all meat, and 29 per cent of all fluid milk. However, these very small operations depended heavily on inputs openly given or clandestinely diverted from the large farms.

Not surprisingly, most workers on collective and state farms had little motivation to work hard and conscientiously for their large organisations. So city-dwellers were often forced to assist specified state or collective farms during the busy seasons of the year. Since the person's regular employer bore the cost of sending such "assistance" to the farms and paid most of his salary during his time in the countryside, this practice had the effect of providing collective and state farms with additional cheap labour.

Many Soviet and Latvian agricultural economists, as well as numerous farm managers and workers, acknowledged that the collective farm system was inefficient and very costly. In the mid-1980s, the central Soviet authorities allowed cautious experiments with the establishment of individual farms, especially in areas with labour shortages or unused production facilities, to supplement the production of the collective and state farms. The Latvian Supreme Soviet used the opportunity to permit the creation of real independent farms, adopting a "Law on Individual Farms" in 1989. That legislation, which went far beyond the provisions of central Soviet legislation, began to lay the legal basis for the restoration of private individual production in agriculture. By 1990, there were more than 7 000 registered family farms operating more than 120 thousand hectares of land. However, Latvian policy shifted in 1990 from one limited to making small changes that only complemented the command agricultural system to one aimed at eliminating it altogether (Table II.3).

Table II.3. **Number and average size of farms, 1 November 1990**

(numbers, thousand hectares)

Farm type	Number	Total area	Agricultural land	Arable land	Average size
Collective farms	411	2 332.0	1 462.6	993.2	5.674
State farms	171	1 213.0	757.0	513.8	7.094
Other state agricultural enterprises	241	184.9	104.3	71.7	0.767
Total large farms	823	3 729.9	2 323.9	1 578.7	4.532
Individual farms	7 296	151.9	108.7	79.1	0.021

Source: Central Statistical Bureau of Latvia (CSBL).

B. Privatisation and transformation in primary agriculture

The institutional transformation of Latvian agriculture that started in 1990 had two main elements: a change in land tenure and ownership (land reform) and the redistribution of the non-land production assets of large, Soviet-era farms to private farmers. The mechanisms put in place in Latvia, unlike those in some NIS, were designed from the outset to bring about the complete dismantling of collective and state farms and their transformation into family farms. Even though legally farms already had the option of becoming corporate enterprises, the reforms on which Latvia embarked in 1990 gave the government several ways in which to actively support the development of a family farm sector.

1. *Land reform in the 1990s*

Land reform actually started in June 1990, after the Supreme Soviet of the Republic of Latvia passed a resolution entitled "On Agrarian Reform". The basic principles of land reform were subsequently embodied in the "Law on land reform in the rural territories of the Republic of Latvia", which was passed on 21 November 1990. This legislation set up a network of land commissions at the national, regional and pagasts level to manage land distribution. The head of the local government normally chaired the commission, whose members were confirmed by the local council. Subject to an appeal to the higher-level land commissions, the pagasts land commission ruled both on what land should be subject to restitution and on the validity of claims to it. The reforms were designed to return land nationalised during the Soviet era to private hands; in principle, all state-owned agricultural land, whether used by collective farms, state farms, household plots, or any other Soviet-era entity, was to be reassigned to other users or possibly privatised.

Former owners and their heirs, current occupants of the land, and persons who wished to receive land and were not employed in agriculture could all apply for a parcel of land. There was no restriction on the amount of land to be returned to private ownership, although where lots of more than 100 hectares were involved, Cabinet approval was required. The legislation allowed for the land to be used for different modes of farming:

- private farms;
- part-time farms;
- household plots.

As in the 1930s, families that wished to farm as a sideline to some other rural business could receive smaller plots for setting up ''part-time'' or ''craftsman's'' farms.[4]

All requests for land had to be submitted by 20 June 1991. The law initially stipulated that all decisions on land allocation had to be made by the end of 1992, by when the commissions were supposed to have prepared new, district-wide land reclamation plans. But that deadline was extended to give time for former owners and their heirs to make claims, since the 1937 Latvian civil code had been restored in the meantime, changing the legal definition of heirs and increasing the pool of persons eligible to file a claim for the return of previously family-owned land.

Conflicting claims were inevitable, since the land reform legislation stipulated that land should be returned to former owners and that current users of the land could file claims. Paragraph one of the ''Law on Land Reform in Rural Areas'' thus set the priorities for fulfilling requests for allocation of non-urban land. Top priority went to claims by the former owner or his heirs. They were to receive the land except in cases where it was occupied by:

- individual full- or part-time farms;
- individual residences, whether currently inhabited or under construction;
- inhabited multi-family residences;
- environmentally protected objects;
- registered historical monuments or archaeological sites;
- local government facilities;
- other social assets;
- experimental farms; or
- plots within legally-defined limits on which there were productive improvements, buildings, or orchards belonging to other owners, including collective and state farms.

Where restitution claims were denied for one of those reasons, the recognised former owner could choose to receive a plot of land of the same size in another place in his pagast or district (or in another district if that was not possible) or alternatively to receive ''compensation'' vouchers under the general privatisation and restitution procedures.

After all requests for land restitution were satisfied or rejected for one or the other of the above reasons, the remaining land was to be allocated:

- to existing individual full-time farms;
- to part-time farms, if the petitioner had a single-family residence;
- to people wanting to build a single-family residence;
- to other individuals for any legally permitted use.

Agricultural land that was not requested for one of these uses reverted to the existing user, usually a collective or state farm, if it was asked for. Thus any approved individual application for land, whether for restitution to previous owners or for a new individual farm, had a higher priority than continued use of the land by a collective or state farm. However, the law also stipulated that even approved claimants for restitution could be made to wait up to five years if the land they claimed was needed by a corporate successor of a collective or state farm for its production. The amount of such land temporarily retained by the large farm was calculated by the commission according to a formula relating the amount of land to the farm's other production assets (for instance, the amount of land needed to grow the feed required for the farm's remaining cows). That allowed the successor of the collective or state farm to continue operating on a reduced scale and to provide its remaining workers with a livelihood while the privatisation of its non-land assets was completed, as described in the following section.

By the end of the legal period for filing land claims, more than 300 000 applications for land use had been submitted for a total of 5.35 million hectares, which was 1.27 times the area subject to land reform. In 1992 alone, 35 000 families applied for a total of 607 000 hectares of land for the immediate purpose of setting up individual farms. By 1996, 75 000 individual farmers had applied for a total of 1.8 million hectares, some of whom had wanted to start operating as early as 1992. Altogether, 100 000 applications were received for 616 000 hectares for establishing part-time farming operations and the same number again applied for 240 000 hectares for creating household plots. Corporate farms spawned by collective and state farms petitioned for a total of 2.7 million hectares, equivalent to 74 per cent of the land that those farms had occupied before reform and 43 per cent of the land subject to reform. Under current legislation, applications from corporate farms were only partly met due to their lower priority.

Some 100 700 claims (36 per cent of the total) were received from former landowners or their heirs seeking restitution of their land. A further 29 per cent of requests for land restitution came from urban residents, while 2 per cent (1 400) came from persons living outside Latvia, mostly in the United States, Canada, Sweden and Germany.

The "Law on Land Privatisation in Rural Areas", passed on 9 July 1992, established the procedures for the second stage of land reform, which officially started on 1 January 1993. During this phase, formal title to land was to be recorded on the basis of land surveys, so that purchase and sale of land could begin. This process was protracted because of the need to prepare further legislation: the law establishing the State Land Service (surveyors) was passed only in December 1992. At the same time, the "Law on the Land Title Register" established the registry as a part of the Supreme Court. Land Title Registry offices began to operate only after 1 April 1993, and the first land title was registered on 31 May 1993. The registration process is likely to take a long time. By November 1994, the Land Register had recorded only 6 144 restituted land titles and 2 468 newly-purchased land titles.[5] By that time, approval had been given for the restoration of ownership rights to 23 900 former owners. By 1 July 1995 there were registered land titles for a total area of 22 100 hectares of rural land.

2. *Privatisation of collective farms' non-land assets*

Privatisation of state and collective farms' non-land assets was carried out in accordance with the provision of the "Law on Privatisation of Agricultural Enterprises and Collective Fisheries", which came into effect on 1 July 1991. This was the first Latvian law that explicitly mentioned "privatisation". It stipulated that "all" the country's collective and state farms were to be privatised. (On 1 January 1991 there had been 623 collective and state farms in Latvia, which each had an average of 3 550 hectares of agricultural land, employed 310 workers, and had 2 350 head of livestock and 55 tractors.)

The privatisation of property was designed both to compensate owners and their heirs for non-land assets forcibly incorporated into the kolkhozy during collectivisation and to reward all farm workers' efforts on the collective farms during the Soviet era. The legislation also sought to maximise the transparency of the distribution process and to minimise disruption of production. By the end of the process, the former collective and state farm organisations were to be abolished as a legal form of entrepreneurship.

The legislation stipulated that the privatisation of non-land assets of collective and state farms be undertaken in two stages. Firstly, the legal status of collective and state farms was to be changed, after which all their non-land assets were to be allocated to farmers and other entrepreneurs and the former collective (state) farms liquidated.

The law provided that a general meeting of each farm's workers was to elect a farm privatisation commission to begin the process of non-land asset privatisation, to approve the farm's statutes and determine how the shares should be calculated. The privatisation commission was to draw up a list of shareholders and their initial holdings, the rules for the transition to corporate farm status, and an inventory of the reorganised farm's property. The commission's proposals had then to be approved by a general meeting, at which participants had first to approve the list of shareholders and their initial shares by voting on the basis of one man, one vote. The general assembly then voted on the other proposals on a pro rata basis according to the shares owned by each member.

The property inventory listed all the corporate farm's non-land assets at a given date (usually 1 January 1992). The property was divided into lots for the purposes of privatisation (see below); a lot might consist of an animal or a single piece of machinery, or of an entire production facility with all its equipment and stock (in theory all the farm non-land assets also could be set as a single lot). Once the assets had been listed and the lots determined, their composition could be changed only with the approval of another general meeting, so there was usually a great deal of discussion about the inventory at the farm general meeting which approved it.

All the state or collective farm's non-land assets were valued at the cost of acquisition or construction. That valuation was then used as the total declared capital of the new corporate farm, which was divided into shares with an equivalent total nominal value that represented entitlements to receive. They were not legal tender or exchangeable outside the group of owners originally entitled to them. Each shareholder had the right:

- to keep the shares for future dividends;
- to sell or give the shares to other shareholders;

- to use the shares to pay for lots of property;
- to invest the shares in the fixed capital of new co-operatives or other business entities created by the corporate farm's shareholders on the basis of operating units from the property inventory.

Shares were given only to farm members and other persons legally entitled to be included in the shareholder list. Other people living and working on the farm and its land, such as workers involved in social and other non-agricultural services, were eligible for shares only in specific cases.

Two criteria determined the proportion of the total share value of the corporate farm to which each recipient was entitled. Firstly, some shares were allocated as compensation for non-land assets expropriated during collectivisation. If the recipient was an heir of or himself a person who had had non-land assets taken during collectivisation, then he could receive shares representing the present value of the property taken. Since these shares were given as compensation, individuals or their heirs who had suffered from collectivisation of their property could receive share entitlements to the farm's property even if they were no longer members of the farm nor resident on its land. Other shares amounting to at least half of the total shares were allotted in proportion to the recipient's contribution to the farm during its operation, usually calculated as the ratio of his total earnings to all wages paid by the farm. In practice, most farms assigned about one-third of their total property share value as compensation for collectivised property.

After the general meeting of shareholders had approved the corporate rules (by-laws), the share list and the property inventory, the collective or state farm was legally reorganised into a new legal entity as either a joint stock or a limited liability company and known as a "corporate farm". The law allowed a collective farm general meeting to opt for rapid liquidation without establishing a temporary company, but that happened only in three cases out of 623. There was also a possibility of reorganising the farm into a co-operative, for which the one man-one vote system of voting had to be used, but finally no farm was reorganised in this way.

Once the new corporation was established, the collective or state farm privatisation commission was dissolved, and the newly-elected corporate board took over the management of the farm and of the property allocation process, subject to ratification by general shareholder meetings. The law stipulated that all former state and collective farms were to be reorganised into corporate farms by 15 March 1992. Although the legislation anticipated (without setting strict time limitations) that all these new legal entities were to exist only for the time required to reallocate all non-land assets. Meanwhile, corporate farms were allowed to file claims for the land they needed to continue operating during that period, which they did, as noted above.

In the second stage, the new corporate farm, once legally organised, could start distributing non-land assets. Any shareholder had the right to claim for any lot or lots of property, at the price fixed in the inventory, paying for it with cash or shares. The corporate farm board was required to make this claim (offer) public within the company immediately. If no one else made an offer to purchase the same lot within one month after the original bid was made public, it went to the first bidder. If other requests to buy the lot were received, then it was sold at a closed auction to the highest bidder from among those persons who had submitted bids. In such an auction, any bidder could require that payment be made solely in shares. Whether the purchase was unopposed or contested at auction, the successful bidder had to pay for the lot within two weeks. If he could not, it reverted to the corporate farm and was offered for sale again.

All shareholders had an unconditional right to make an offer for any lot in the inventory. Once the list of lots had been approved, the corporate farm could not withhold any lot from sale even if it seemed necessary for the corporate farm's continued operation, nor could it refuse to sell if the person asking to buy possessed enough shares (either his own or a group's) to pay the asking price.

The total capital of the corporate farm and the number of its shareholders progressively decreased during the privatisation process, although the nominal value of a single share (entitlement) could effectively increase. A shareholder who used all his shares to purchase physical property lost his rights as a shareholder. Similarly, when there was an auction for a particular lot, the nominal value of the shares bid could be higher than the lot's inventory value, leaving fewer shares available for the purchase of remaining lots. In order to preserve the balance between the nominal value of outstanding entitlements and the nominal value of the remaining non-land assets to be distributed, share values had to be reviewed at least once a year by a general meeting of the shareholders.

Despite that revaluation process, the increasing nominal value of entitlement shares did not necessarily make it advantageous to hold one's entitlement unused and remain a member of the corporate farm. The most attractive lots were likely to be sold first. They were also the ones most likely to be contested, and so they sold for much more than their inventory value. Remaining items were thus likely to be less desirable and sell for a lower price. Indeed, the board could, with the general meeting's consent, reduce the asking price of lots which did not sell in order to dispose of them. During the privatisation process, therefore, unredeemed shares could even lose their initial face value. Once all lots from the inventory were purchased in this way, the law required the farm's shareholders to decide formally to liquidate the enterprise.

To promote the privatisation of the farm sector, in 1992 the Supreme Soviet of the Latvian Republic approved legislation providing for old debts to be written off in the process of redistributing corporate farm assets. Under this provision, old long-term debts (contracted before privatisation) were distributed to the total value of shares. When a share was used to privatise the non-land assets to individual property the related debt was paid from the State budget.

In many cases, corporate farms which disposed of all their non-land assets still had outstanding debts to the state electricity utility ''Latvenergo''. In such a case, the corporation had to go through a court proceeding, involving a three month waiting period before it could be liquidated. The time-consuming procedure to put a formal end to these indebted shell farms may explain why so many former collective and state farms that had passed liquidation resolutions were not actually dissolved in 1994 and 1995, although they had long ceased operation (Table II.4).

Table II.4. **Collective and state farm transformation**

Date	Total number	Had been liquidated and deleted from the Company Register	Had passed liquidation resolution	Operating
1 January 1991	616	0	0	616
1 November 1993	613	16	293	304
1 January 1994	613	18	330	265
1 January 1995	613	120	301	192
1 June 1995	613	133	303	177

Source: Latvian State Committee on Statistics. Ministry of Agriculture of Latvian Republic, Annual report, 1995.

Data on the sale of non-land assets were recorded up to January 1994, when the Latvian Central Statistical Committee stopped collecting information from former state and collective farms. By then, about 69 per cent of companies' assets had been privatised.

The available data indicate that lots consisting of single items were sold more quickly than lots comprising complete operating units, such as a cow shed with its livestock and equipment. In some instances, unwanted empty buildings remained on large livestock farms, while their livestock was sold separately. One reason why individual items were sold more quickly than complete production units was probably the difficulty of gathering the number of shares needed to buy the entire unit. But early purchasers were willing to go through the auction process and pay more over the inventory valuation for individual lots. In many cases, early buyers later sold the machinery or livestock for cash on the open market.

As the sale of non-land assets proceeded, however, the price paid for lots declined to around their inventory value. This change clearly reflected not only the adjustment of share values described above but also the fact that the most desirable items were sold first.

In an attempt to stop the break-up of large farms, the law on the privatisation of non-land assets was amended in May 1995, giving these corporate farms the possibility of retaining non-land assets needed for their continued operation. Under the new law, the general meeting had to approve the separation of property from the corporate farm itself. That alteration of privatisation legislation went against the goals set in the original laws, which were clearly designed to encourage the sale of corporate farms' non-land assets to individuals or groups of individuals. It was clearly stated that the corporate farms created out of the old collective and state farms were a transitional structure that existed only as long as it was necessary to privatise all their non-land assets. Current legislation makes it possible for corporate farms to remain in business, so long as their general assembly is in favour and they prove their viability.

3. *Problems in land reform and decollectivisation*

The "Law on the Privatisation of Agricultural Enterprises and Collective Fisheries" governing the privatisation of non-land assets often came into conflict with the "Law on

Land Privatisation in Rural Areas''. There were instances when land commissions allocated land to the former owners or to new users, usually for the establishment of new individual farms, leaving the production facilities of former collective farms, generally livestock units, without land and hence unable to operate. Similarly, there were cases where farmers who had received land under the 1989 law creating individual farms lost it again as a result of the introduction of the 1990 law on general land reform.

The ''Law on Land Privatisation'' granted corporate farms that had been given land for permanent use in the first stage of land reform the right to use the land for five years (ending in 1997). Production units were thus able to continue operating even if there was a restitution claim against the land occupied by the farm's facilities. But as soon as those production facilities were privatised as non-land assets, the restitution claim took effect. So if a corporate farm shareholder purchased an asset such as a cattleshed, he could lose the land on which it stood as soon as he bought it and so be unable to use it. That was a real problem and remained so in 1995, according to the Latvian Ministry of Agriculture, since the previous legislation conflicted with new legislation relating to the privatisation of certain types of non-land assets (buildings and constructions). It meant that there had to be a lease or purchase contract between the owner of the privatised non-land asset and the owner of the land on which it was built before such assets could be privatised.

Since the right to use the land expires in 1997, by when all claims for restitution are to be settled, it is unclear how the problem of all corporate farms' remaining non-land assets will be resolved. Moreover, as mentioned previously, there are measures preserving the use of these non-land assets for these corporate farms, but their right to hold on to the land they are operating against the claims of individuals expires in 1997, and the means for settling such disputes remain unclear.

As yet, there is no effective market for the sale or lease of agricultural land in Latvia. So it could happen that an individual farmer acquires a cowshed with 200 cows without having any real possibility of getting enough land to produce the feed he requires. The only option remaining to him would be to buy the feed on the market.

One of the basic obstacles to creating an effective land market is the time taken to register land because of the lack of staff in the state authorities responsible for land registration. The fact that so little land has been registered so far also reflects the problems of getting land accepted as collateral for bank loans, which are badly needed to finance the modernisation of the farm sector. In areas with good conditions for agricultural production, banking and credit institutions do accept registered land as collateral for loans.

4. *Post-reform farm structure*

The restructuring and privatisation of agriculture have engendered fundamental changes in the structure of Latvia's farming sector. In 1990, state farms accounted for about 31 per cent of agricultural land use and collective farms for 61 per cent. By

January 1995, about 17 per cent of land was farmed by corporate farms (operating an average of 706 hectares) and 46.7 per cent by family farms (averaging 19.9 hectares in size), while 22.7 per cent was occupied by part-time farms (5.2 hectares) and 9.2 per cent by private plots (two hectares) (Table II.5).

By the beginning of 1995, there were a total of 656 corporate farms, which was more than the number of collective and state farms before reform. Of the more than 600 corporate farms created out of the former collective and state farms, only 192 were still operating at the beginning of 1995. The Latvian Ministry of Agriculture expected only 120 or 130 of these corporate farms to still be operating at the beginning of 1996. All other corporate farms were liquidated during the privatisation process, once all their non-land assets had been sold to private individuals. The 1995 amendment to the law on the privatisation of corporate farms' non-land assets could help the remaining corporate farms originating from collective farms to continue operating.

During the privatisation period, other corporate farms were established in one form or another by individuals using privatised assets. By 1 January 1995, there were around 464 of these new corporate farms operating autonomously in a free market environment.

Altogether, at the end of 1995 there were some 650 corporate farms, whether newly created or the successors of collective and state farms, operating a total of 62 600 hectares, representing 17 per cent of all agricultural land in Latvia. Large-scale farming is thus playing a minor role in total agricultural production.

The individual farms that emerged from land reform and the privatisation and restructuring of Latvian agriculture are now the cornerstone of the country's agricultural sector, occupying 81 per cent of total agricultural land. In 1995, 64 364 family farms averaging 20 hectares occupied 46.7 per cent of all agricultural land in Latvia, while part-time farms and private subsidiary plots accounted for a further 32 per cent. Although it is very hard to separate market-oriented farming from self-subsistence farming, in the current situation some 40 per cent of agricultural land is probably operated by farms that are not oriented to market production and whose operators rely on other sources of income.

Table II.5. **Structure of agricultural land use in Latvia, 1 January 1995**

Type of farms	Number of farms	Total Agricultural land thousand hectares	Average area per farm, hectares	Share of total agricultural area, %
Family farms	64 364	1 278.7	19.9	46.7
Part-time farms	118 749	620.5	5.2	22.7
Private plots	124 736	251.6	2.0	9.2
Private orchards	65 037	7.0	0.1	0.3
State farms	95	52.0	547.0	1.9
Corporate farms	656	463.0	706.0	16.9
Other	4 149	62.6	15.1	2.3
Total	377 786	2 735.4	7.2	100

Source: Central Statistical Bureau of Latvia (CSBL).

As regards the allocation of resources amongst the different types of farms, major changes have also taken place in recent years. At the beginning of 1993, corporate farms used most of the tractors in Latvia, but by the end of 1994 almost three-quarters of the country's tractors were operated by individuals. Much the same has happened in the case of other farm machinery and technology. Moreover, livestock production has followed a similar pattern: at the end of 1992, two-thirds of the country's total cattle herd were owned by corporate farms, but by the end of 1994 individual farmers possessed two-thirds of the total cattle and four-fifths of the cows.

The primary privatisation process has more or less been completed now and further structural changes in the size and nature of farms will arise as new owners acquire both land and non-land assets. Further changes will be limited by registering land ownership in the Land Title Register. The state has retained ownership of agricultural land that has not been transferred into individual private ownership.

5. *Effects of privatisation and transformation on sectoral performance*

The performance of the agricultural sector between 1991 and 1995 was affected not only by sectoral privatisation and transformation but also by the general reform of economic and political processes introduced after Latvia regained independence. Since it is hard to assess the effects of these general factors on agricultural performance, the specific effects of the privatisation and transformation of the sector are also difficult to evaluate.

The main feature of the sector's performance in 1991-1995 was the decline in production. Whereas the fall in animal production was mainly due to the loss of the NIS market, the drop in crop production was more closely related to the effects of land reform and the privatisation and transformation process. There was a particularly sharp reduction in the area of land used for arable crops, especially in 1994 and 1995, when the area sown to crops fell by 16 per cent and 22 per cent respectively. Relative to 1990, the area sown to arable crops in 1995 was 43 per cent down (Table II.6).

Within the farming sector, family farms have the smallest proportion of their total land area sown to crops (Table II.7). However, it is not possible to say whether land not

Table II.6. **Land for arable crops**

	Units	1990	1991	1992	1993	1994	1995p
Sown area	*'000 ha*	*1 627*	*1 621*	*1 572*	*1 426*	*1 195*	*930*
Change over previous year	per cent	–	99.63	96.98	90.71	83.80	77.82
Change over 1990	per cent	100	99.63	96.62	87.65	73.45	57.16
Change over previous year	'000 ha	–	6	49	146	231	265
Change over 1990	'000 ha	–	6	55	201	432	697

p: provisional.
Source: Central Statistical Bureau of Latvia (CSBL).

Table II.7. **Distribution of total agricultural land and sown area in 1994**

Group	Agricultural land thousand hectares	Sown area thousand hectares	Sown area as % of agricultural land
Corporate farms	515	293	56.89
Family farms	1 279	436	34.09
Part time farms and subsidiary plots	872	466	53.44
Total	2 666	1 195	44.82

Source: Central Statistical Bureau of Latvia (CSBL).

sown to arable crops has become permanent grassland or pastureland, or is simply left idle. It can nevertheless be said that the main achievement of the privatisation and transformation process has been to transfer the bulk of agricultural production to individually owned farms.

In 1992, individual farms accounted for 42 per cent of all cultivated land, and by 1994 that proportion had risen to 75 per cent. In 1994, 71.5 per cent of cereals, 65.8 per cent of sugar beet and 96.5 per cent of potatoes were produced by private individual farmers.

As far as livestock production is concerned, private individual farmers accounted for 77 per cent of total milk production in 1994, and their average milk yield was about 10 per cent higher than that of corporate farms. However, the large corporate farms still bulked large in pig and poultry production in Latvia, accounting for 46 per cent and 67 per cent respectively.

C. Privatisation in the upstream and downstream sectors

1. *Situation during the Soviet era*

a) *Upstream industries*

With the exception of the agricultural machinery industry, the Ventspils liquid fertiliser plant and agriculture-related services, Soviet Latvia had no industries producing inputs for agriculture. Inputs were supplied through centralised state agencies which generally had a single office in each rural district with monopoly rights to supply the farms in that district. Each type of service was handled by a separate enterprise with its own centrally-determined plan.

For instance, mineral fertilisers, pesticides and other agrochemicals produced elsewhere in the USSR were distributed in Latvia by the local branch of the Soviet *sel'khozkhimia* (agrochemical) agency, while another central agency, *sel'khoztekhnika,* had a monopoly on the sale and repair of agricultural equipment. Some other services, such as most farm construction, were provided by "inter-farm enterprises", which usually covered an entire rural district but were nominally owned by the farms themselves.

Because these upstream enterprises were accountable to planners in Moscow and Riga and were not responsive to the needs of their customers, farms, like other Soviet-era enterprises, sought wherever possible to develop in-house capabilities in services such as equipment repair and construction.

b) *Downstream industries*

Under the centrally planned economy in Latvia, as in other former Soviet republics, there was a strictly centralised system of buying and processing all products from agricultural enterprises. Before 1991, the centralised grain supply system in Latvia was based on a low selling price and a correspondingly low purchase price. All grain trade depended on obligatory state purchase orders, which were fixed for almost every agricultural producer irrespective of its efficiency. Obligations had to be fulfilled in the autumn.

All marketable grain resources were stored in centralised state storage facilities, which simultaneously processed the grain into feed or baking flour. There were 15 such enterprises in Latvia with a total capacity of about 750 thousand tonnes per year. These enterprises were engaged in both upstream and downstream activities (downstream as grain processors and upstream as suppliers of animal feed mixtures for the livestock sector).

The Latvian system had its own peculiarities. Agricultural enterprises specialised in cattle production used grain purchased from outside Latvia, so only 20 per cent of all grain grown in Latvia had to be marketed to the state. The remaining grain was used by farms as feed. Besides grain storage facilities, therefore, Latvia had an extensive network of grain processing and storage facilities on collective and state farms. They carried out the initial processing, storage and milling, but did not usually produce quality mixed feed. Grain was normally delivered to state feed-producing enterprises for processing into concentrated feed and farms had to pay a service fee.

The country was divided into 10 dairy processing regions, each of which had a centralised dairy processing enterprise. All these large dairy enterprises were state owned and covered the whole of Latvian territory, albeit with shared service zones. These were the main manufacturers of dairy products, producing evaporated or condensed milk, butter and cheese. Each of these central dairy processing enterprises (*kombinats*) received raw material from several dairies in its district. The latter collected milk from the farms and undertook the first stage of processing, producing milk for consumption, butter, and certain types of cheeses. They either sold their output directly to consumers in their local district or supplied product to the central unit for further processing.

State and collective farms and other small producers had only one milk collection and processing enterprise to which to deliver their milk. The price they received was fixed by the state and all dairies paid that same price for their milk.

Meat processing was concentrated in 14 plants, two of which, in Riga and Valmiera, processed more than half of all meat produced in Latvia. All but two owned by the collective farms were state owned. Each enterprise had its own collection district (''catchment area'') and the plants to which farmers had to supply product were strictly determined. The enterprise in its turn had to buy all production from the district and pay a price fixed by the government. Live animals were delivered to the large meat processing plants equipped with slaughtering facilities, which then produced finished cuts of meat for retail sale.

Some 60 000 tonnes of meat were exported annually to the large cities of the USSR. Because of a lack of investment in new technology during the Soviet period, production equipment in meat processing plants is now obsolete. Seven of the plants do not have deep freezing storage capacities.

2. *Privatisation of upstream and downstream industries*

a) *Privatisation of upstream industries*

As has already been said, apart from the agricultural machinery industry and the liquid fertiliser plant in Ventspils, Latvia had no industrial plants producing inputs for agriculture. The privatisation of these large enterprises was subject to the same laws and regulations as other state-owned industrial enterprises. As the privatisation of these sectors was very slow, only one of these enterprises had been privatised by the end of 1995.

However, there were also many small production units that were part of large agro-service enterprises and were specialised in the production and/or repair of different types of agricultural machinery. Almost all the machinery needed in agriculture, excluding tractors and combined harvesters, was produced in small series by these plants, which were privatised under the same procedures as other agro-service enterprises.

Agro-service enterprises were privatised under the terms of the ''Law on Privatisation of Assets in Agro-Service Enterprises'', passed on 30 March 1993. This law provided for agro-service enterprises to be split into smaller independent companies, which were then privatised. Their shares were to be sold on a quota basis, with about 50 per cent to be offered to farmers' co-operatives (although they did not exist in all areas). The main criterion for fixing quotas was the volume of business done with the enterprise being privatised. Shares offered to farmers' co-operatives but not taken up, together with the remaining 50 per cent, were to be offered firstly to employees of the enterprise and then to other individuals.

Each unit to be privatised was sold individually in a separate operation, either under an immediate purchase contract or under a leasing contract with a subsequent right to buy during the following three to five years. The 122 enterprises that originally existed in the agro-service sector were broken down into 871 units for privatisation. By 1 November 1995, 797 of them had been sold, while the remaining 73 (mostly the larger units) were in the process of being privatised.

b) Downstream enterprises

Different procedures were used for privatising the dairy, meat and other processing industries, depending on factors such as historical tradition, technology and processing enterprise structure. The privatisation of agricultural processing and agro-service enterprises in Latvia started in 1993, following the passing of the necessary legislation:

- "The Law on the Privatisation of Dairy Processing Enterprises" – 19 January 1993.
- "The Law on the Privatisation of Assets of Agro-service Enterprises" – 30 March 1993.
- "The Law on Sugar" – 11 May 1993.
- "The Law on the Privatisation of Meat Processing Enterprises" – 18 June 1993.
- "The Law on the Privatisation of State Bakeries" – 1 July 1993, which was amended in 1994 to establish the rules for the privatisation of grain processing enterprises as well.

Under these various laws, plans were drawn up for privatising the enterprises concerned and specific procedures were established for each one. The privatisation plans were individually approved by the Ministry of Agriculture or by a privatisation commission authorised by the Ministry (Table II.8).

Dairy sector

The changes in the dairy sector started even before the Law on the Privatisation of Dairy Processing Enterprises was passed. The situation in the sector changed fundamentally in 1991, when the state stopped purchasing milk and it was bought instead by dairy processing enterprises acting as economically independent entrepreneurs, albeit still state owned. The catchment areas of the former period were also abolished, so buyers of dairy products started offering varying prices and dairy processing enterprises had to compete for markets. The scope for exporting dairy products was also substantially curtailed.

Table II.8. **Privatisation results in the main food industry sectors in Latvia**

Food industry sector	Number	1 January 1994		1 November 1995	
		Privatised	Started privatisation	Privatised	Started privatisation
Dairies	15	1	14	15	–
Slaughterhouses	14	1	–	11	1
Bakeries	14	1	–	13	1
Grain processing factories	17	–	1	7	10
Sugar factories	3	–	–	2	1
Technical service enterprises	871	–	871	797	73

Source: *Annual Report on Agriculture*, Latvian Ministry of Agriculture, 1995.

All local smaller dairy processing plants were privatised in 1992. The procedure used was designed to achieve one major goal – to link milk producers closely to the processing industry.

Under the provisions of the "Law on Privatisation of Dairy Processing Enterprises", adopted by the Supreme Council of the Republic of Latvia on 15 April 1992, privatisation was to be carried out in two stages:

Stage 1

The ownership of some local dairies was transferred to revived and newly established Dairy Farmers' Associations, which were set up under the by-laws on Dairy Farmers' Associations and the "Law on Co-operative Associations", passed on 6 August 1991. Since July 1992, about 170 dairy farmers' co-operative associations have been formed in Latvia. Their geographical area of activity was generally decided on the basis of 1 940 territories. The new by-laws on dairy farmers' co-operative associations were modelled on the 1937 by-laws, approved by the Cabinet on 17 December 1937.

Since 1992, the small, local dairy enterprises that collect milk and carry out first stage processing, of which there are several in each district, have mostly been privatised as co-operatives. Their ownership was transferred, without compensation, to the dairy farmers' co-operative associations on the basis of their claims. Thus, dairy producers were given the opportunity to choose the level of their co-operation system.

As competition in the market for dairy products intensified over the following years as a result of the ongoing restructuration and privatisation process, some of the privatised local dairies were bankrupted. But total production capacity in the dairy processing sector still outstrips the current level of milk production in Latvia.

Stage 2

The "Law on Privatisation of Dairy Processing Enterprises" was passed in January 1993, laying down the framework for the privatisation of the 10 large central dairy plants. They were to be transformed into joint stock companies, with specific quotas set for the distribution of shares: dairy producers' associations were to hold at least 70 per cent; employees were allowed no more than 10 per cent; the remaining 20 per cent was to remain in the hands of the state. Milk producers' co-operatives also had the right to purchase shares for vouchers or cash. As the whole process had to be completed within seven months, milk producers were obliged to establish local dairy producers' associations within that short period of time.

Under the provisions of this legislation, the above-mentioned 10 large central dairy processing enterprises (one in each district) were transformed in 1993, into joint stock companies in which the main shareholders were dairy farmers' co-operative associations. These enterprises attracted most of the investment in dairy processing in the years before privatisation, and their plants are now capable of processing most of the milk produced in Latvia and high value added products. These enterprises or their subsidiaries are likely to continue producing most of the dairy products produced in Latvia for the foreseeable future.

Unlike the privatisation of local dairy plants, ownership of which was transferred without compensation to dairy co-operatives, the shares of the large dairy processing enterprises were sold to the dairy co-operatives for between 25 and 50 per cent of their nominal value. However, the proceeds were not paid into the state budget but were directly invested in the privatised enterprise.

The state's holdings in these privatised enterprises may be sold to private interests at a later stage. The decision as to whether to purchase the state's shareholding rests not with the state (the formal owner) but with the new private owners of the company. They can decide on the date and the form of purchase, and must invest the proceeds in the company.

By the end of 1995, the privatisation of all 15 large state-owned processing companies created from the 10 centralised enterprises of the former period had been completed. The main problem in that process was the weak financial situation of the agricultural sector, which resulted in a lack of cash for investment and left farmers (dairy co-operatives) unable to purchase shares. There remains the problem that the processing co-operatives, the main shareholders in these companies, lack not only capital but also technical, marketing and business skills, which may hold back the development of a downstream industry that is so vital for the prosperity of agriculture.

Meat processing

In the second half of 1992, a framework for competition was created in the meat processing sector. Geographic processing zones disappeared, and the enterprises that offered the highest prices to producers and paid most promptly took the largest volumes.

Some small private meat processing businesses were established in 1993 and 1994, which used small-scale equipment usually bought for credits provided for the purpose under different assistance programmes. Small companies in meat processing and marketing were expected to develop rapidly and to change the market situation in the meat processing sector. They provided real competition for the large unprivatised meat processing plants, especially given that demand for meat was declining. But since the privatisation of the former, state-owned enterprises in 1995, the resulting large private companies have essentially determined general market conditions.

When the legislation governing the privatisation of the meat processing sector was being drafted, a conflict of interests erupted between farmers' associations and the employees of meat processing enterprises which complicated the primary objective, i.e. to create flexible, privately-owned and market-oriented companies. Differences emerged as to who should acquire meat processing enterprises and the price at which each enterprise should be sold.

Farmers' associations wanted to acquire these enterprises for nothing and to create meat producers' co-operatives (as had happened in the dairy sector in the case of smaller local dairy plants). At the same time, the employees of the enterprises concerned sought to purchase at a low price the entire capital, or at least a majority shareholding, of the joint stock company created out of the state enterprise.

In May 1993, the Supreme Council passed the "Law on Privatisation of State Meat Processing Enterprises", which stipulated that privatisation should be completed within a relatively short timeframe. Unlike the legislation covering the dairy sector, it specified that the main buyers should not necessarily be farmers' co-operatives but the bidder that had proven ability to manage a competitive business.[6]

The law provided for each enterprise to be privatised in two stages:

- Formal reorganisation of the state enterprise into a state-owned, joint stock company.
- Sale of shares to private persons according to special rules and quotas, to be laid down by a privatisation commission:
  - employees up to 10 per cent;
  - state pension fund up to 10 per cent;
  - farmers 25 to 35 per cent, to be divided amongst meat producers wanting to buy shares according to the size of the business or the land it used. Moreover, meat producers that had outstanding debts to a state meat processing enterprise (having not paid for animals delivered) were able to acquire shares up to that value free of charge;
  - the main shareholder (the "general entrepreneur") at least 51 per cent of the capital. This holding was to be sold to the highest single bidder in an auction. There was no particular definition of the main shareholder; it could be an individual or a company, but it was presumed to be the owner of the majority of the privatised enterprise and hence its decision maker.

The main shareholder was to be selected by open tender, and all would-be purchasers had to propose a business plan. The law provided that if bids were received from more than one possible "general entrepreneur", the privatisation commission had to decide whose business plan was the best. Nevertheless, all potential buyers were to be allowed to participate in the auction of the shares, but those that had proposed less satisfactory business plans were subject to a 20 per cent surcharge on the auction price.

Holders of the main lot of shares who acquired shares in the privatisation process had to pay only 20 per cent of the nominal value of their shares in the first year; the rest to be paid within three years. If no potential buyer came forward at the asking price for the shares, the price was reduced.

By 1 November 1995, 11 of the former 14 state meat processing enterprises had been fully privatised, while one was still in the process of being privatised and two had been liquidated instead of being privatised. The main problem involved in privatising the meat processing sector was its low capacity utilisation rate and its outdated technology.

Grain processing sector

In the former Soviet period, Latvia's grain processing sector (for human consumption and also for feed) was heavily dependent on supplies from the all-Union fund and received most of its grain from other Soviet Republics (especially from Russia, Ukraine and Kazakstan) via the central supply agencies. In 1991 and especially 1992, the situation changed radically. Cheap, state-subsidised grain supplies ceased and domestic grain prices rose sharply, making grain production a highly profitable business. One effect of high prices was to stimulate local supply, but it also increased the cost of livestock production.

Privatisation was carried under the amended "Law on the Privatisation of State Bakeries", which basically applied the same principles to the privatisation of grain processing enterprises as those applied for the meat industry and state bakeries. The main difference was that, for grain processing enterprises, greater preference was given to grain producers' co-operatives or associations in the privatisation process. The law stipulated that at least 51 per cent of shares should be offered to, and then purchased by, farmers' co-operatives or associations of agricultural producers. As a general rule, producers' co-operatives or associations of producers were offered 60 per cent shareholdings in the privatised enterprises.

In 1992, when the previous fixed collection and supply areas were abolished and individual enterprises began to compete, state-owned grain processing enterprises started to operate as independent businesses. The real process of privatising state-owned grain processing enterprises started only in 1994. However, compared with the privatisation of the dairy and meat processing sectors, it has been slow. By 1 November 1995, only seven of the 17 former state-owned enterprises in the sector had been successfully privatised, while privatisation of the other ten was under way.

Under the system of centralised state control, about two-thirds of Latvia's total grain storage capacity was located on collective farms. Those facilities and related grain handling plants were the basis for the establishment of rural district grain processing and storage operations, which were mostly co-operative enterprises. Until the establishment of separate private enterprises, these operations remained in the hands of the new companies created out of the former collective farms.

The privatisation of the 14 state-owned bakeries started in 1993, when a special law was passed. It laid down similar rules for the privatisation of bakeries as for meat processing enterprises, with the exception that part of the shares could be sold to farmers as a special group.

By 1 November 1995, the privatisation of 13 of the former state-owned bakeries had been completed, while the last one was in the process of being sold. At the same time as the large bakeries were privatised, new small bakeries were set up to cater to niche markets.

Sugar refining

There are three sugar plants in Latvia, which all have sugar processing and refining capability. Refining of domestically-produced sugar beet meets 40 per cent of the country's sugar consumption. To meet domestic demand in full and to use their refining capacities effectively, the three plants mostly process imported cane sugar and export refined sugar. Hence, the refiners are not heavily dependent on the supply of raw sugar beet from domestic producers.

The framework for the privatisation of sugar plants was laid down in a decree promulgated by the Latvian parliament on 11 May 1993, which gave some preference to farmers as regards the allocation of shares and payment terms for them. By 1 November 1995, two of the three plants had been fully privatised, while the sale of the third was going ahead.

As in other sectors where preferential terms for the sale of shares to farm associations were granted, the main problem was the inability of farmers to participate in the privatisation of these enterprises due to their lack of capital.

c) *Privatisation and structural changes in wholesale and retail trade*

In the former command economy, the "wholesale" sector played only a limited role that was unrelated to the market. The main wholesale functions, such as storage and distribution to retail stores, were carried out directly by food processing enterprises in their "spheres of interest". The state-owned wholesale companies had very limited storage and transportation capacities and mainly handled administrative tasks such as book-keeping and the registration of shipments from food processing plants to retail outlets. The retail business included state-owned shops, which were usually operated by the same firm or organisation that handled wholesale distribution.

Consumer co-operative enterprises (*Turiba*) engaged in wholesale or retail distribution existed in parallel with the state wholesale and retail sector. The co-operatives ran collectively-owned wholesale (storage and transportation) facilities and a network of retail units. There were co-operatives covering most of Latvian territory outside the seven major cities.

In the process of privatisation, the state-owned wholesale distribution organisations were abolished and state-owned retail outlets were privatised, usually through direct sale by auction between 1991 and 1994.

Co-operatives still operating in wholesale and retail distribution now have to compete with privatised and other emerging firms in the market. They have managed to survive by selling some of their assets (warehouses, shops, stock, and so on) to private firms and individuals.

Newly established firms consist mostly of import-export organisations that also engage in wholesale distribution and supply imported products and, to a limited extent, locally produced products to local retail shops.

At the same time, a large number of new private retail shops have been established, especially in major cities. In addition to permanent retail establishments, street markets have also developed rapidly. They obtain their merchandise from the above-mentioned newly established import-export firms, as well as directly from processing companies and from farmers that avoid going through wholesalers so as to keep the distribution margin for themselves. According to some estimates, these street markets account for more than one-third of total retail turnover.

"Interpegro" is the only major new private company combining wholesale and retail distribution to have been created. In contrast to the situation in the central European transition economies, no large foreign agro-food companies have entered the sector so far in Latvia.

Part III

AGRICULTURAL AND FOOD POLICY OBJECTIVES AND MEASURES

A. Agricultural policy framework

As the Latvian economy has been progressively transformed from a command system into a market-oriented system, the main goals of agro-food policy have altered accordingly. Although policy instruments have changed more slowly, this systemic transformation underlies the entire discussion of specific policy measures that follows in this part of the report.

1. *Policy framework under Communism*

The overall purpose of Soviet-era farm policy was to ensure a guaranteed, if minimal, supply of foodstuffs to the population, especially in the cities. The authorities pointed to the existence of regular urban food supplies and the low and unchanging retail prices for foodstuffs – set in the 1930s and raised only in 1962 and again in the late 1980s – as decisive evidence of the command system's success.

After 1965, when the Soviet authorities began officially to commit massive resources to agricultural and rural areas, the improving quality and quantity of food supplies, particularly of meat and dairy products, were routinely cited as a justification of the system's right to exercise political dominance over the peoples of the USSR as well as a top priority of the authorities. The Baltic republics' agricultural sectors, like those of their neighbour Belarus, were oriented by the Moscow planners to provide maximum supplies of meat and milk to the large north-western Russian cities, particularly Moscow and St. Petersburg (Leningrad), located in zones of mediocre agricultural potential.

As we want to illustrate the development of the main agricultural policy instruments used in the Soviet period, in the transition period and recently, we will not analyse in detail all the instruments used during the Soviet era. Instead, they will be summarised at the beginning of each specific policy sector.

2. *New agricultural policy objectives*

The restoration of the Latvian Republic as a sovereign state and the decision to move to a market system brought a fundamental change in agricultural policy objectives. One of the main goals was to bring about a relatively rapid transition from the system of state procurement and state controlled prices to a system of real market prices with minimal state involvement in the agro-food market.

Another strategic objective was to privatise and transform the collective and state farms in a relatively short time. The declared objective of this policy was to convert the agricultural sector into one based primarily on individual private farming. This objective was also supported by a selective use of different types of agricultural policy instruments.

In the privatisation and restructuring of the upstream and downstream sectors, the principal objective was to abolish the state monopoly and to promote competition between enterprises (especially in the downstream sector). In the dairy sector (the largest), a specific objective was established as part of the privatisation process – to closely integrate milk producers and the milk processing sector. (For more details on the privatisation and transformation of the agro-food industry see Part II).

The restoration of Latvian sovereignty also had an effect on the country's agriculture insofar as it deprived it both of supplies of inputs and of the traditional outlets for its output, as the Russian cities suddenly became foreign territory. In addition, conflicts over appropriate levels of income and support in agriculture were expected to become more intense during the transition period, so one of the less explicitly defined objectives was to ease the process of adjusting the Latvian agro-food sector to the new domestic and international market conditions.

During the transition period, a new policy objective was adopted – to integrate Latvian agriculture into the international agro-food market. To that end, Latvian policy-makers decided it was necessary to put in place a sufficient level of border protection for Latvian agriculture to enable it to meet competition from countries with more heavily subsidised agricultural production.

More recently, agricultural policy has emphasised the need to provide consumers with a higher quality of healthy food products, whether domestically produced or imported.

a) *Discussion on future agricultural policy*

In 1994, the Latvian Ministry of Agriculture started to develop a long-term strategy for the agricultural sector. That led to the publication in 1995 of the first of what are to be annual reports on the situation in Latvian agriculture. Moreover, an "Agriculture Bill" was introduced and debated in the *Saeima*. The main objective of these two initiatives was to create a framework for formulating a coherent agricultural policy that is have three main goals:

- improving social, regional and environmental conditions in rural areas;
- increasing the competitiveness of Latvian agro-food products;

- introducing an income support scheme for farmers that complies with Latvia's international commitments under various agreements and treaties.

The declared objective of the Agriculture Law is to maintain the participation of agriculture in the development of the national economy by means of a consistent, long-term policy for the agricultural sector and the establishment of mechanisms for its implementation. It calls for agricultural policy to be targeted on promoting the three main functions of farming: the production of agricultural commodities, the maintenance of sustainable rural communities, and the safeguarding of the environment. More specifically, that means:

- supporting the development of rational agricultural enterprises producing commodities at reasonable prices;
- developing an economically stable and environmentally concerned agricultural sector;
- preserving natural resources and offsetting the natural and economic inequalities in agriculture by, amongst other things, giving equal social and income opportunities to people engaged in agriculture and forestry.

There is considerable ambiguity surrounding these objectives, especially as regards the implementation of agricultural policies that are designed to attain all the declared objectives. Moreover, the equal income opportunity concept creates some concerns, since in many other countries policies aimed at income parity through price regulation have proven to be very costly and largely unworkable. It would thus seem preferable for income objectives for rural areas to be more targeted and incorporated in rural development policies rather than sought through market distorting price policies. Hence, instead of specific agricultural policies designed to achieve these objectives (basically by supporting production), a more broad-based, long-term policy of rural development should be considered.

3. *Overview of the main instruments of agricultural policy*

The agricultural policy instruments applied during the privatisation and restructuring of the agro-food sector and its adjustment to new market conditions can be divided into three main categories:

Measures enshrined in the legislation setting out the rules for the privatisation and transformation of the agro-food sector. In addition to general privatisation legislation, specific regulations were applied to the privatisation of agriculture and downstream industries (see Part II).

Policy instruments associated with the transition towards a more market-oriented economy, such as:

- abolition of subsidies on agricultural inputs;
- elimination of all consumer subsidies from the previous period;
- gradual liberalisation of agricultural producer and consumer prices;

- establishment of minimum prices, which were not enforced by state regulation of the market but applied by state food processing enterprises;
- creation of a system of border protection.

Measures associated with enhancing the quality of the commodities produced and the health and safety aspects of agro-food products, which included:

- introducing regulations for improving the quality and safety of chemical and other inputs;
- providing subsidies for the use of high quality inputs, such as high quality seeds and animal breeds;
- creating a legislative and institutional framework for ensuring the quality, health and safety of agricultural and food products.

There are no specific rules for state intervention in the market. During the transition period, export subsidies were used only in 1994 and for a limited range and for specific volumes of products. As mentioned earlier, the state protects the domestic market through border protection (at rather a high level for livestock products in particular) and the application of ''minimum'' prices (solely for grains since 1993).

a) Future agricultural policy instruments

The present draft of the new Agriculture Law provides the following main instruments:

- border protection;
- targeted subsidies to improve the technological level of agricultural production and thus improve efficiency and competitiveness;
- the use of state reserves, i.e., government intervention, to stabilise the market;
- provision of (investment) assistance to bring product quality up to international quality and food safety standards.

No specific instruments for income support are envisaged, since the underlying approach is not to provide income-oriented price support but to top up low incomes by direct payments.

The law calls for the government to submit to parliament an annual report on the situation in agriculture, which must include a description of short and medium-term policy aims and the mechanisms for their implementation. The government's report and the annual agriculture law must also specify the budgetary allocations required, all of which must be approved by parliament.

B. Price and income support measures

In describing the price system and support policies applied in Latvia since 1986, the following distinct periods can be identified:

- the era of strict regulation, which ended in 1990;

- the early transition period, when there was still state control over agricultural prices, although input and output prices rose sharply, with inputs going up more than farm products;
- the subsequent introduction of free market prices on 10 December 1991, although price controls were maintained on the main agricultural products;
- the beginning of price stabilisation in 1993, with prices essentially determined by the market (with the exception of grains and sugar beet).

1. *Soviet period of strict regulation*

Up to 1990, there were two main types of state support for agricultural producers and consumers of agricultural products, both effected through the system of state-set, obligatory procurement prices for required deliveries to state agencies. On one side, state prices were differentiated to reward higher levels of production and plan fulfilment, while on the other side a complicated system of ''additional payments'' to farms was designed to ensure farms a minimum level of return in order to preserve them as functioning economic and social units. The government also pursued a strict retail price policy, that kept consumer prices relatively low and stable.

The system of additional payments was introduced to stimulate agricultural production, because total output was inadequate.

Under the centrally planned economy, prices were set at four main levels:

- Procurement prices for agricultural products, used for all sales of agricultural products to the central government. They were fixed centrally but were not uniform, since there were wide regional variations reflecting differences in natural conditions and estimated production costs.
- Wholesale prices, also fixed by the state and applicable to sales by processing enterprises or wholesale trade organisations to other enterprises or organisations.
- Retail prices, applicable to goods sold to final consumers. They were set by the central government, with those for food normally very low. Changes in retail prices (as for all prices fixed by the government) could be made only by governmental order.
- Agreement prices, which were freely determined by producers and consumers. However, under the centrally planned system, these prices were applicable to a limited range of products and volumes.

All prices apart from agreement prices were imposed either by the USSR State Price Committee (and by the Council of Ministers in the case of some of the most important products) or by the Latvian State Price Committee (as regards the prices of less important products), or by ministries (for prices applicable to industrial or technical sectors).

a) *Procurement prices*

Procurement prices were applied to the purchases of the main agricultural products produced by state and co-operative agricultural enterprises. Not only collective and state farms but also private households sold agricultural products such as grain, beef, pork, poultry, eggs and milk at these prices, mainly to processing enterprises.

Procurement prices were adopted for a five-year period, but fixed on an annual basis. However, marketing products was not a problem as demand exceeded supply. In addition, state processing enterprises were willing to purchase everything produced by farms. There was also a rather complicated price support scheme.

Differentiated procurement price system

To take account of the differences in the economic situations of farms, it was decided in the 1960s to differentiate procurement prices for the main products.

Then in 1983, a system of procurement prices with four price categories for agricultural products was introduced (Category I offered the highest prices to agricultural producers and Category IV the lowest). All agricultural enterprises were placed in one or other of these price categories on the basis of economic criteria such as level of profitability and natural conditions (quality of soil, climate and other factors). Paradoxically, under this system an agricultural enterprise producing under favourable natural conditions could only be placed in Category I on the grounds of poor economic performance and thus be "rewarded" by higher prices.

Moreover, supplementary price payments were introduced to help unprofitable farms. On 14 March 1983, the State Government Price Committee drew up a list of unprofitable farms for each agricultural region, specifying additional percentage payments on top of the fixed prices for the main agricultural products (see Table III.1, Columns "2"). The additional payments ranged from 5 per cent to 50 per cent of the procurement price, depending on the farm's profitability. (The list was confirmed by a resolution of the Council of Ministers of the Latvian SSR and was subsequently amended and updated several times.)

Supplementary price payments were also made on top of procurement prices (50 per cent of the procurement price) for the amount procured over and above planned deliveries as a means of stimulating the supply of larger volumes (Table III.1).

This complicated system of payments and supplementary payments resulted in individual prices being fixed centrally for almost every farm. It was a combined price and income support policy that was intended to stimulate agricultural output (with greater importance attached to quantity than quality) with no consideration for production costs and efficiency.

b) Wholesale prices

In the Soviet system, wholesale prices for agro-food products sold to the retail trade were not fixed but calculated as the difference between fixed retail prices and strictly regulated trade margins, set according to the category of enterprise and the type of goods. These trade margins were set for all kinds of goods to cover the presumed selling costs and to ensure a minimum profit for the distributor. For products not sold at the retail level, such as agricultural inputs, fixed wholesale prices were applied.

Table III.1. **Total value of additional payments for main agricultural products in Latvia**

(thousand Russian roubles)

Products	1986		1987		1988		1989		1990	
	1	2	1	2	1	2	1	2	1	2
Grains	5 730	1 384	7 519	959	8 979	3 127	9 797	3 584	–	–
Sugar beet	593	218	549	240	3 028	7 066	1 864	5 624	1 227	4 343
Flax	532	490	1 245	616	741	3 181	1 543	3 728	336	1 611
Potatoes	2 512	–	1 037	–	905	6 325	1 792	7 711	–	575
Vegetables	29	–	–	–	371	15	218	–	4	–
Other crop products	302	–	852	–	529	2 880	504	1 637	276	438
All crop products	9 698	2 092	11 202	1 815	14 553	22 594	15 797	23 505	2 074	7 074
Milk	54 864	42 897	63 483	40 465	62 581	133 890	63 939	132 410	36 696	75 832
Cattle	36 243	36 136	42 734	24 037	42 030	180 689	37 054	171 200	17 799	81 067
Pigs	23 873	17 745	29 601	15 972	31 719	36 805	28 753	38 395	10 892	17 084
Sheep	1 315	1 550	1 267	285	1 190	5 712	961	5 429	323	1 559
Poultry	8 493	1	9 390	–	11 136	–	1 736	–	5 999	–
Other livestock products	37	–	50	–	65	2	42	9	19	13
All livestock products	124 825	98 329	146 525	80 759	148 721	357 098	132 485	347 443	71 728	175 555
Total	134 523	100 421	157 727	82 574	163 274	379 692	148 282	370 948	73 802	182 629

1. 50% supplementary payments on the prices on agricultural products.
2. Additional payments for non-profitable farms.

Source: Central Statistical Bureau of Latvia (CSBL).

Since the retail prices of food products were not changed, nor were the corresponding wholesale prices. Increases in production costs were offset by direct payments made from the state budget, the amount of compensation being the difference between the calculated price and the fixed wholesale price. These payments were made under the responsibility of the relevant ministry and overseen by the Ministry of Finance. This system of compensation payments from the state budget had the objective of maintaining wholesale and retail food prices at fixed levels (regardless of increases in production costs) and were effectively consumer subsidies.

c) *Retail prices*

Stable consumer prices for food were one of the basic goals of all centrally planned economies. Any changes in retail food prices were thought to be politically damaging and had to be approved by central government. Over the past decade, however, economic problems have necessitated increases in food prices, which up to 1990 were camouflaged by the introduction of terms such as "goods of first necessity", "delicacy", and "luxury goods".

d) Agreement prices

At the beginning of the 1980s, the Soviet Union started to liberalise the price system, beginning with the abolition of procurement prices for fruits, vegetables and later on potatoes. This meant that all these products could then be sold either to governmental or co-operative enterprises at agreed prices or directly to consumers via the local market.

2. *The transition period*

During the short transition period (1990-91), radical changes were made to the agricultural price and income support system. In 1990, when deep-seated economic changes were taking place in Latvia, the Council of Ministers continued to set fixed procurement prices, but for a smaller list of products. All other income and price support mechanisms, including the system of differentiated prices and supplementary payments, were abolished.

The early reform period, which followed the restoration of Latvian independence, was characterised by hefty price increases because the Soviet Union stopped supplying inputs such as fuel and fertilisers at low prices and supplies had to be imported at something akin to world prices. The second factor behind the general rise in prices was price liberalisation. At the same time as input prices soared (especially compound feed, fuel, fertilisers, agricultural machinery and equipment and building materials), agricultural output prices also rose, but less rapidly. The government was obliged to raise procurement prices twice, once on 1 January 1990 and then in June 1991, to partially offset the input price increases that had inflated production costs.

One lesson from the relatively short transition period was the clear failure of government attempts to compensate farmers for the sharp rise in input prices by increasing procurement prices. This was the general feeling at the time and it was the farmers themselves who demanded the replacement of procurement prices by free market prices for agro-food products. The government subsequently decided on 10 December 1991 to deregulate agro-food prices.

Both wholesale prices and retail prices were liberalised during the transition period when the state continued to set maximum wholesale and retail margins only for the most important products.

3. *Introduction of market prices*

Under Council of Ministers resolution No. 350 "Concerning prices on food products", adopted on 10 December 1991, all food and other agricultural products had henceforth to be sold at market prices. As part of the complete liberalisation of all prices the government set so-called minimum prices for grains, livestock products, sugar beet and flax, and the state guaranteed to purchase these products at the minimum price. The price guarantee was not imposed by specific regulations but was applied by the state food processing enterprises, which were ordered to pay at least the minimum price for the products they purchased.

The government set up price agreement councils in each processing enterprise, which included the representatives from agricultural, processing and trade organisations. The prices the enterprise had to pay to farmers were decided weekly by the councils and were clearly not market determined. The decision on the prices to be paid was not taken by central government, therefore, but was the product of an untransparent system of price fixing introduced at a time when the supply and demand balance was not the corrective mechanism and prices were still fixed arbitrarily.

This ''liberalisation'' of market prices led to a substantial increase in farm gate prices. The biggest increases took place in 1992 (when cattle went up 3.8 per cent per month, pigs 14.4 per cent, poultry 13.9 per cent and milk 11 per cent). In 1993, prices continued to rise, but less rapidly (Table III.2). For grains, moreover, prices were much lower in 1993 than the year before, since prices in 1992 had been set extremely high (increasing the cost to livestock producers, especially of pigs and poultry) and the resulting drop in demand led to a subsequent fall in grain prices despite the minimum price.

Wholesale and retail prices were meant to be determined only by market conditions. The attempt to consult a variety of groups when deciding the price paid to farmers by the processing industry obviously conflicted with the market forces provided by wholesale and retail markets. Wholesale and retail prices increased sharply in 1992 (wholesale prices for beef meat increasing at a rate of 8.5 per cent per month, pork at 17 per cent, poultry at 14 per cent and milk at 19.8 per cent), which dampened consumer demand and led to more moderate price increases in the following years.

Table III.2. **Prices paid to farmers in 1990-1995**

(LVL per tonne)

Products	1990	1991	1992	1993	1994	1995p
Wheat	1.16	5.01	95.28	48.90	49.00	70.30
Rye	1.51	4.26	99.95	41.50	39.20	53.00
Barley	1.33	4.56	92.84	38.20	37.60	43.30
Oats	1.31	4.72	82.61	40.50	48.70	47.10
Potatoes	1.71	7.18	41.20	45.00	47.00	70.00
Sugar beet	0.35	1.28	17.68	21.78	21.15	21.00
Beef and veal (liveweight)	14.69	28.94	111.18	174.20	311.20	377.50
Pigs (liveweight)	14.79	27.37	244.08	607.00	846.10	839.80
Milk	1.99	3.92	38.28	60.45	70.20	85.90
Poultry (liveweight)	14.92	26.70	208.45	767.30	969.90	930.30
Eggs (1 000 pieces)	0.60	1.63	12.67	26.13	28.20	34.00

p: provisional.
Source: Latvian Institute of Agricultural Economics.

Prices stabilised to some extent in 1994 and 1995, when agricultural prices rose by less than the overall rate of inflation. Farmers maintained that prices did not cover their production costs, but consumers' reduced purchasing power and the very high share of household spending devoted to food limited the scope for price increases.

The minimum prices for agro-food products introduced during the transition period (in 1991) soon became irrelevant as a result of shifts in relative price levels and were abolished at the end of 1992. Since 1993, grains have been the only main commodity for which the government has maintained minimum prices, but there has been no mechanism providing a real price guarantee to producers. Sugar beet producers were given real price guarantees in 1992-1994, when the Ministry of Agriculture fixed the minimum price at LVL 20 per tonne (plus transport costs) and required state-owned sugar plants to abide by it.

4. Price and income support by commodity

a) Grains

Grain is the main Latvian crop product and covers some 45 per cent of arable land. Due to poor climatic conditions, production of winter cereals is limited. Hence, only a small proportion of cereals (winter wheat with a sufficient gluten content) meet quality requirements for human consumption and most cereals are used for animal feed. Only about 15 per cent of total grain production was used for human consumption, meeting 20 per cent of domestic demand. However, according to the Grain Bureau, the proportion of human grain consumption met by domestic production has increased to 40 per cent in recent years. Spring barley is the most important grain in Latvia, accounting for about 50 per cent of the grain area. It is primarily used for feed as well as, to a limited extent, for malt production. The other major grain produced in Latvia is wheat, also mostly used for feed. There are appreciable yearly fluctuations in grain output, and at less than two tonnes per hectare, average grain yields are very low relative to those obtained in OECD European countries and even in the CEECs.

Important changes in the grain output are characteristic for the recent period. The evolution of grain area and production in 1994 and 1995 shows a sharp decreasing tendency. The total grain production in 1994 fell by 27 per cent over 1993, and the estimates of the 1995 grain production are lower again by 23 per cent over 1994. In both years the production fall is due principally to lower area sown for grains.[7]

As of 1993, grain was the only main commodity where minimum prices were still in force, but there was no mechanism providing a real price guarantee to grain producers. Nevertheless, the Grain Bureau can influence the market situation by buying for stocks at the minimum price and selling later on the market. The Grain Bureau can also import grains at a zero tariff rate, which gives it a virtual monopoly on grain imports, since other importers have to pay the import tariff of 25 LVL (US$48) per tonne for grains for human consumption and 75 LVL (US$144) per tonne for feed grains. The Grain Bureau imports approved volumes of grains, which in 1994 and 1995 amounted to 90 000-95 000 tonnes of wheat for human consumption and 180 000 tonnes of feed grain.

The minimum price is set below world market prices, around US$90 per tonne, but the Grain Bureau also imports grain at lower prices than that. In the spring of 1995 grain was imported from Kazakstan at US$60 per tonne, while wheat for human consumption was imported from Ukraine at US$155 per tonne plus transport costs.

b) Oilseeds

Traditionally, oilseeds are not an important crop in Latvia. In view of climatic conditions, the principal oilseed suitable for cultivation in Latvia is rapeseed, with a planted area of around 0.1 per cent of total arable land. Taking account of the very low level of self-sufficiency in edible oils and protein feed and the fact that rapeseed is suitable for less favoured conditions, given that it has a potential yield of 2.5 tonnes per hectare (which is a realistic expectation for Latvia), rapeseed has undoubted possibilities in Latvia, especially since it requires no special technology. The main obstacle is the lack of oilseed processing capacity.

As far as price support is concerned, none has been applied to oilseed since 1991, when the procurement prices of the Soviet period were abolished. The higher price paid to domestic farmers is thus due to protective measures and imperfections in the market.

c) Sugar and sugar beet

Because production conditions for sugar beet are poor in Latvia, it is cultivated on a very limited area and in only a few parts of the country. Before 1991, the sugar beet area was 13 500 to 14 600 hectares (i.e., about 1 per cent of total arable land). The expansion of the area to 24 800 hectares in 1992 was due to increased production on private household plots. That temporary increase was brought about by a government scheme prompted by the substantial shortfall in sugar production in the previous years. The scheme introduced in 1992 provided for producers of sugar beet to receive a certain volume of sugar in exchange for sugar beet, and that encouraged owners of household plots to increase sugar beet production. However, the operation failed because of problems in transporting the output of so many producers from their household plots to processing plants. As a result, the area sown to sugar beet plunged to around 12 000 hectares in 1993 and 1994 and to only 9 500 hectares in 1995. Because of higher yields in 1995, sugar beet production increased by almost 10 per cent over 1994, but still remained low compared to previous years.

In the Soviet period, Latvia produced between 40 and 50 per cent of the sugar it consumed from domestically produced sugar beet. More recently, the proportion has fallen to about 30 per cent. Large volumes of raw cane sugar are imported for processing in local refineries, and the refined sugar is mostly supplied to the local market, although some is exported. The government's target is to increase sugar beet production to a point where domestic production covers 75 per cent of consumption.

Up to 1994, the price for sugar beet was set by the Ministry of Agriculture and remained stable at 21 LVL between 1992 and 1994. The price remained at much the same level in 1995, moreover. Since the privatisation of all three sugar plants in Latvia is supposed to be completed in 1996, the state can no longer provide direct price support by fixing the prices that processors must pay for sugar beet. Instead, price support will continue to be provided through border protection. At present, the import tariff is fixed at US$200 per tonne, equivalent to a rate of 60 to 70 per cent.

d) Potatoes

Potatoes are the most important non-grain crop in Latvia, accounting for around 5 per cent of arable land in the Soviet era and for almost 7 to 8 per cent in recent years. A large proportion of output is not marketed but is retained by farms for both animal feed and human consumption. No specific price support or market regulation mechanisms are applied to potatoes. The only indirect price support is provided by border protection, with a tariff of around 20 per cent.

e) Milk and dairy products

As mentioned above, the dairy sector was and still is the most important sector in Latvian agriculture. In the Soviet period, production far outstripped domestic demand. As for the other livestock sectors, the objective of the transformation process was to bring output into line with market demand. Between 1990 and 1995, cow numbers were reduced by 45.5 per cent and total milk production fell by 50 per cent. Milk yields, which declined from 1990 to 1992, increased slightly and then stabilised during the 1993-1995 period, although milk production declined by 6 per cent in 1995.

There is no specific price and market regulation system for milk and dairy products, and the transition to a free market brought a substantial drop in prices. Because of continued state involvement in the price-setting system during the transition period, the dairy sector in particular and the livestock product sector in general were adversely affected by high grain prices set by the state. Since 1993, however, the only price support to the sector has been provided by border protection. Dairy products are part of a group of products – together with beef and pigmeat – for which tariffs are relatively high at around 40 to 50 per cent.

f) Livestock and meat

There were even greater changes in meat production than in the dairy sector. Between 1990 and 1994, total cattle numbers fell by 72 per cent and pig numbers by 64 per cent, although up to 1994 pork production fell more rapidly than beef production. Pork production, which was mostly concentrated in large-scale production units, was dependent on imports of concentrated feed. In response to increased feed costs and reduced export opportunities, pig breeding and fattening activities were substantially reduced between 1990 and 1993.

Lower grain prices and higher production margins (especially on pigs, given that the producer price of pork was about twice that of beef) in 1993 and 1994 had an effect on herd numbers in 1994 and 1995, when they stabilised and even started to increase again. There was a modest 4 per cent increase in the pig herd in 1994 and a further 11 per cent rise in 1995. Cattle herds continued to contract in 1994 and 1995 (by 19 and 3 per cent respectively). Beef and veal meat production declined continuously from 1990 to 1995. Beef meat production in 1995 was equivalent to 38 per cent of 1990 output. Between 1990 and 1994, production of pigmeat fell even more sharply than that of beef, and pigmeat production in 1994 was only 39 per cent of the 1990 level (as against 54 per cent in the case of beef). In 1995, however, pigmeat production recovered, rising by 9 per cent relative to 1994.

As with milk and dairy products, price support for beef and pigmeat is provided indirectly through border protection, since imports of these products carry one of a high level of customs tariff.

g) Poultry and eggs

The poultry sector was also concentrated in large production units. During the transition period, it had to face low output prices as a result of reduced domestic demand and export opportunities as well as of an increase in feed and energy prices. Over the 1990-94 period, the poultry flock fell by 64 per cent, while poultry meat production dropped by 72 per cent and egg production by 56 per cent. In 1995, the poultry flock increased by 11 per cent over 1994, but poultry meat production declined by a further 5 per cent, although egg production increased by 17 per cent.

There is no price support and market regulation mechanism for poultry and eggs. Since 1993, no institutional prices have been set for any product apart from grains and sugar beet. Measures in support of agricultural prices are confined to border protection. Tariffs on poultry and eggs in 1995 were at much the same level as those for the main crops, but lower than those on dairy products, beef and pigmeat.

C. Market protection

1. Soviet era

During the Soviet regime, all foreign trade was centrally controlled and import and export decisions were not made at the enterprise level but at the level of the central planning authorities. Hard currency export earnings were centrally collected and used for financing centrally planned imports. All export and import operations were handled by state monopoly agencies often specialised by industrial sector.

As far as Latvia was concerned, it exchanged large volumes of agro-food products with the territory of the FSU, but they were not real exports and imports. Nevertheless, that trade and its development during the period of transition and economic reform were important for the Latvian agro-food sector and its restructuring. In the Soviet era, Latvia did not have international trade relations and was unable to be a member of international trade institutions and agreements.

2. *The transition period and current situation*

In 1990, Soviet foreign trade was decentralised to some extent and all 15 Soviet republics were given the right to manage their own foreign trade. As a result of these changes, the Latvian SSR initially created its own set of monopoly foreign trade organisations, emulating the disbanded Soviet agencies. The main instruments of the newly designed policy were agreements stipulating international trade on a bilateral or multilateral basis. Border protection measures were also introduced.

Another goal of the new trade policy was to restrict or eliminate dangerous agro-food imports and low quality products. Trade regulations providing welfare, health and food safety protection are based on the "Law on the Protection of Consumer Rights" and the "Law on Food". Under this legislation, mandatory requirements concerning consumer health and environmental safety are subject to certification in accordance with the procedures laid down by the Cabinet. Similar legislation governs the safety of imported agro-food inputs (such as chemicals and fertilisers). The National Foodstuff Certification Centre and the State Machine Experimental Station issued instructions regarding certification of foodstuffs and other products.

A list of goods subject to certification was approved by the Latvian Cabinet. Selling goods on the list without a certificate is forbidden. Certification procedures comply with generally accepted international regulations and mutual agreements between trade partners, and certificates are issued by the Certification Centre of Foodstuffs. Imported goods subject to certification are controlled by customs.

a) *Import measures*

Import tariffs

Under current trade policy, the basic instrument for market protection is customs tariffs. A new law on tariffs was passed on 15 October 1994 and came into force on 1 December 1994. It lays down tariffs for imports (and any export charges) of specific goods. Under this legislation, different sets of tariff rates are applicable for each of the three trade regimes (other than the free trade regime):

- basic rates (standard regime);
- rates for the most favourable trade regime – MFN treatment;
- other preferential rates for different kinds of preferential quota trade, covered by specific trade agreements (Table III.3).

To protect Latvian agricultural producers, import tariffs on agro-food products are relatively high compared with rates of duty for other goods. There are differentiated tariff rates on agricultural products:

- From 0.5 to 1 per cent for goods not produced in Latvia (basically tropical zone products).
- 20 per cent[8] for products in which Latvia has a low level of self-sufficiency (crop products, live animals and meats excluding beef and pork).

Table III.3. **Import tariffs for the main agro-food products in 1995**
(per cent or LVL per kg)

Commodity	Basic rate	MFN rate	Preferential rates granted to EU	
			1995	2000
Cattle	40%	30%	30%	24%
Pigs	55%	45%	45%	24%
Sheep and goats	40%	30%	30%	24%
Fresh, chilled and frozen beef	40%	30%	30%	24%
Fresh, chilled and frozen pork	55%	45%	45%	24%
Condensed milk, cream with sugar	40%	30%	30%	24%
Milk powder	40%	30%	30%	24%
Cheese and curd	55%	45%	45%	36%
Butter and other milk fats	55%	45%	45%	36%
Wheat, wheat-rye mixes LVL/kg	0.025	0.025	0.025	0.020
Other grain LVL/kg	0.075	0.075	0.075	0.067
Sugar LVL/kg	0.120	0.120	0.120	0.100

Source: Latvian Institute of Agricultural Economics.

- 40 to 55 per cent for sensitive products in which Latvia has a high degree of self-sufficiency (beef and pork, milk and dairy products). There is also a high level of border protection for grain and sugar, in which Latvia is not self-sufficient (Table III.3).

The main objective of government policy is to balance supply and demand in the domestic market, ensure a relatively high level of protection, and give price support to products of which Latvia has an abundant supply as well as to products that are considered to be the key activities of Latvian agriculture. However, the high level of market protection for the core products of Latvian agriculture isolates producers from world market signals and in the long term will result in a lack of competitiveness. It is a policy which protects the interests of agricultural producers at the expense of consumers, whose interests also need to be considered.

Import quotas and import licensing

The "Law on Custom Tariffs" provides for Latvia to impose tariff rate quotas on all tariff lines. At present, preferential tariff quotas are applied only to imports from the European Union under the Latvia-EU Free Trade Agreement. The preferential tariff quotas with the EU, and any tariff quotas established in the future, are allocated between importers on the basis of public tender by the Customs Tariffs Consultative Council established by the Cabinet. So far, no non-preferential tariff quotas for tightly limiting imports have been applied.

Regulation No. 20 on "Protection of the local market for agricultural products" of 17 January 1995 was issued by the Cabinet in accordance with the transitional rules of the "Law on Customs Tariffs". These temporary regulations were introduced as a temporary measure in 1995 before new legislation on the protection of the domestic market came into force. These regulations applied to the main commodities such as grain, milk, meat, fish, potatoes, and to all derivatives. Under this temporary legislation, the authorities assessed the domestic market situation, and if imports were considered likely to destabilise the market, they recommended that import licensing be introduced. On the basis of that assessment, the government set import quotas for specific products for a period of up to 12 months.

For specific commodities, companies have to apply for a licence to trade. Import licences are subject to several laws; for example, under the ''Law on Entrepreneurial Activity'', products currently subject to import licensing include ethyl alcohol and spirits, tobacco and sugar.

The Spirits Monopoly Board, in application of the ''Law on Entrepreneurial Activity'' and the regulation governing the ''State Monopoly of Spirits and Alcoholic Beverages'' of 25 January 1994, issues licences for alcoholic beverages, spirits and vinegar. Every enterprise that has submitted an application for a spirits or alcohol import or export licence, backed by the required documentation, and whose business activities comply with Latvian law can obtain a licence from the Spirit Monopoly Board.

The Ministry of Finance, in application of the ''Law on Entrepreneurial Activity'' and in accordance with the regulation on the ''Sale of Tobacco Products'' (14 April 1994), issues licences for the following goods: tobacco and manufactured tobacco substitutes, cigars, cheroots, cigarillos and cigarettes from tobacco or tobacco substitutes. Any firm that has furnished all the necessary documents required by Ministry of Finance regulations and which conducts its business in accordance with Latvian law is eligible for a tobacco import licence.

The Grain Bureau, in application of the ''Law on the Latvian Grain Market and State Grain Reserves'' (18 May 1993) issues licences for the following goods: cereals; products of the milling industry; malt; starches; wheat gluten; residuals and waste from the food industries; mixed feed and feed concentrates. Tenders for cereal import licences are required only when there is a proposal to import more than 1 000 tonnes of a specific product. For that, firms have to submit the necessary documentation within the specified time period. In other cases, every firm whose business activities comply with the legislation and which furnishes the required documentation is entitled to an import licence.

The Ministry of Agriculture, in application of decisions of the Licensing Commission and in accordance with the ''Law on Entrepreneurial Activity'', the ''Law on Sugar'' (11 May 1993) and the regulation on the ''Procedure for the Issuing of Special Licences for Sugar Wholesale Sale and Import'', issues import licences for cane or beet sugar and chemically pure sucrose.

b) Export measures

Under the ''Law on Custom Tariffs'', government export incentives can be provided under several schemes:

- financial assistance for production or export development;
- governmental preferential purchases exported with subsidies.

Export subsidies have not been a major instrument of trade policy up to now. They were used to a limited extent in 1994 and early 1995 on a narrow range of products. More specifically, the government provided export subsidies for cheese, butter and grains in 1994 and early 1995. The total cost of these subsidies was LVL 1.7 million (US$3 million) in 1994 and LVL 0.8 million (US$1.4 million) in 1995.

A system of export licenses existed in the early stage of transition. However as some consequences of this system were to tax producers, reduce foreign exchange earnings and limit new export market opportunities, it was abolished in 1992.

D. Reduction of input costs

1. *Credit policies*

Under the Soviet regime, credit systems did not play an economic role for producers. Short-term credits to finance the running costs of farms were advanced at very low interest rates and investment credits were given only to finance the investments decided by the central planners. Under that kind of system, credits had a limited economic role as no real financial market existed.

During the transition period, credit became scarce, especially long-term funding. For agriculture in particular, credit became more expensive and very scarce. At the beginning of the transition, substantial loan finance was made available to agriculture. At the end of 1992, lending from the banking system to agriculture represented about 25 per cent of total credit to all sectors. About 90 per cent of the total consisted of short-term credits, while the remainder was classified as medium-to long-term. Credit was generally provided by branches of the Bank of Latvia (BoL) and practically none was advanced by the emerging private banks. In view of the high rate of inflation, the commercial banking sector focused on short-term operations (credits for no more than three months) and was reluctant to provide the longer-term facilities necessary for investment in agriculture. Practically no long-term credits have been granted to agriculture since 1992. In an attempt to support investments in agriculture since then, the government has created several institutions. Due to the general lack of domestic credit and a lack of government funding, these projects were financed by credits from foreign governments and international organisations.

a) Rural Development Fund (Agroinvest)

Between May 1992 and November 1994, a specially established state company called Agroinvest provided low-interest credits to individual farmers from the proceeds of the sale of US food aid. During that period, Agroinvest advanced credits totalling LVL 980 000 (US$1.7 million) to around a thousand individual farms at an interest rate of 7 per cent.

On the decision of the Cabinet, Agroinvest was liquidated in November 1994 and a Rural Development Fund (RDF) was established as a state-owned joint stock company to provide credits for the promotion of rural activities as a whole. The main objectives of the RDF are to support Latvian rural development, improve agricultural efficiency and create new jobs in rural areas, as well as increase the quality of agricultural products. Under RDF regulations, the fund's activities can be financed from grants out of company profits, foreign aid, and international agencies. The RDF makes its credits available at lower interest rates than commercial banks – 6 to 10 per cent for agriculture and 10 to 20 per cent for non-agricultural activities. In 1995, it extended credits totalling around LVL 2 million (US$3.8 million). Its credits are conditional on a satisfactory economic evaluation of the project and the provision of collateral in the form of real estate or bank guarantees. Registered agricultural and forestry land is also accepted as collateral.

b) Agriculture Finance Company (Laukkredits)

A state credit agency called the "Agriculture Finance Company" (AFC) started operating in January 1994. Its main function is to channel World Bank loans to agriculture. With a central office in Riga and seven local offices, the AFC covers all of Latvian territory. Its credits are provided after a rigorous assessment of the project, and it requires the borrower to put up 20 per cent of the cost and to furnish collateral equivalent to 150 per cent of the value of the loan. The AFC charges a fixed interest rate of 14 per cent, which is set by the Ministry of Finance (commercial interest rates averaged 24 to 28 per cent in 1995). The credits were mainly used to finance purchases of agricultural machinery, especially from Russia, and investments in dairy cattle with a high milk yield. In 1994 and 1995 it disbursed credits totalling LVL 2.9 million (US$5.2 million), and the recovery rate of its credits was around 90 per cent.

c) Latvian state mortgage and land bank

The Latvian state mortgage and land bank was set up in 1993 to provide medium- and long-term credits on mortgage contracts, and to represent the state in land dealings within the land privatisation process. The bank also provides commercial credits, but at rates linked to the interest rates it charges on bond issues. Its interest rates averaged 28 per cent in 1993-94, but were down to 22 per cent by the end of 1995 (since bond rates also fell from 20 to 14 per cent). It provides credit on preferential terms for purchases of tractors and combine harvesters. Five-year credits can be advanced for tractors and seven-year ones for combine harvesters, at preferential interest rates of 8 to 10 per cent in both cases. The bank accepts agricultural and forest land as collateral for loans, but the loan coverage is only 30 to 40 per cent of the mortgage value of the land.

Because of the shortage of credit and the delays in land registration (credit can be given only with the security of property registered in the Land and Real Estate Register), the establishment of this institution was not enough to resolve the agricultural sector's recent credit problems. However, in the future the bank's credits will be important for farmers, since they will be able to raise loans against property. Land mortgaging can help mobilise resources for investment in agriculture once the sector is stabilised and land reform completed, including the creation of a real land market.

2. *Input subsidies*

During the Soviet period, input subsidies were one of the most important instruments for lowering agricultural production costs and maintaining low and stable prices for food. These input subsidies led to widespread price distortions in the whole agro-food chain.

Under economic reform, all input subsidies from the Soviet period were abolished and the artificially low prices of inputs were increased sharply to bring them up to world levels (fuel, chemicals, fertilisers, and so on), which worsened the terms of trade for Latvian farmers. The government made several attempts to provide temporary support through input subsidies, which were designed to give farmers the resources to buy inputs rather than to keep input prices low.

In 1992, the government introduced an additional subsidy for gasoline as a support measure for farmers. Because of sharp increases in input costs, the government decided to provide financial support to producers and to help them complete the sowing campaign. Before the 1992 planting season therefore, a private company called Lears Ltd. purchased fuel on behalf of the government, mostly at market prices and using state guaranteed credits, and re-sold it to farmers. The farmers had to pay only 20 per cent in the spring, with the rest due after the harvest. These fuel credits were only partly repaid, though, and the total cost to the state budget was LVL 4.8 million (US$8 million). A similar system was operated for grain seeds in 1993. The seeds were advanced in kind from state seed fund reserves before the sowing season on condition that they were returned to the fund after the harvest. But again the rate of reimbursement was low.

In 1994 and 1995, a governmental support programme for agriculture provided direct payments to farmers using high quality seeds (direct payments on a per hectare basis) and high quality breeds of animals (payments per head). The objective of this policy was to improve the quality and productivity of agricultural production. These input subsidies were worth LVL 5 million in 1994 and an estimated LVL 5.5 million in 1995.

3. *Tax policy*

a) *Soviet period*

Only three types of taxes were levied under the Soviet system:

- a personal income tax paid by individuals;
- a social insurance tax paid by enterprises out of their gross profits (5 per cent) and a social maintenance tax of 2.4 per cent of their wage bill;
- an enterprise profit tax.

A profits tax was payable by enterprises, but the regimes differed as between collective farms and state farms. Collective farms with a profitability (profit/costs ratio) higher than 15 per cent had to pay a tax of 0.3 per cent for each percentage point of profit, subject to a ceiling of 25 per cent of total profits. For state farms, total profits and undistributed profits were taxed individually at rates set for each particular enterprise.

New tax legislation was introduced in 1990, but it lasted only a short period as a new Latvian tax system came into force on 1 January 1991, when the foundations of the current system were laid. This system was reformed in 1994-95 to reflect the structural changes in the economy in general and in agriculture in particular.

b) Current situation

The new taxation system applied to agriculture is based on the following taxes:
- personal income tax;
- profits tax;
- social tax;
- value-added tax (turnover tax up to 1995);
- land tax;
- fixed assets (property) tax.

Under the Latvian tax system, tax reliefs are provided to stimulate agriculture production. Some of these were reduced or abolished under an amendment introduced in 1994 and 1995.

c) Personal income tax

Up to May 1995, individual farmers, householders and private auxiliary farmers were not liable to pay income tax on incomes earned from agriculture. For other activities, income tax was set at 25 per cent of taxable income. Under the new legislation, agricultural incomes are taxed. Personal income tax is payable on earnings from agricultural activities exceeding LVL 3 000 and on all other non-agricultural profits. Private farmers must also pay personal income tax, if the annual turnover of their farm does not exceed LVL 45 000.

d) Profits tax

Before 1995, major profits tax concessions were granted to the farm sector. Profits tax was not payable on incomes from activities in agriculture, from the processing of self-produced agricultural products and from the production of spare parts for equipment used in agriculture. Taxable profits may be reduced by 30 per cent in upstream industries producing agricultural equipment for use in Latvia. Profits from construction activities on private farms were also exempt from taxation.

Since 1995, private farmers whose turnover in the previous year was less than 45 000 Latis have been exempt from profits tax, but they are liable for personal income tax. Other agricultural enterprises are entitled to a tax deduction of LVL 10 per hectare of land used in agriculture, and also have the possibility of applying for a so-called small enterprises discount of 20 per cent.

e) Social tax

Before 1990, employers did not pay social tax. Pensions were paid from the state budget or from the resources of collective farms. With effect from January 1990, enterprises became liable to pay a social tax on behalf of their employees at rates linked to wage levels in their particular sector. The lowest rates applied to agriculture (4.4 per cent), while much higher rates applied elsewhere (e.g., 18.2 per cent in industry, 15.6 per cent in the construction sector). But this regime was only applied in 1990.

In January 1991, a new social tax was introduced:

- 1 per cent was payable by individual employees out of their incomes.
- A tax was payable by enterprises as a percentage of their wage bill. For enterprises engaged in agriculture and in the processing of their own agricultural production, the tax rate was 18.5 per cent of the wage bill, and double that (37 per cent) in other sectors.
- Self-employed farmers have to pay the social tax for themselves and for the members of their family employed on the farm. They pay a rate of 19 per cent of at least two minimal wages.

f) Value Added Tax

Latvia introduced a value added tax (VAT) on 1 January 1995 in place of the ormer turnover tax. The standard rate of turnover tax was 12 per cent to start with (and 18 per cent with effect from November 1993), but a rate of only 6 per cent was payable on basic agricultural products from 1992 to November 1993, which was raised to 10 per cent up to July 1994. After that, a flat rate tax of 18 per cent was applied.

Private farms with turnover of less than the equivalent of 2 000 minimal wages were exempt from the turnover (VAT) payments up to May 1995. Under the new law that took effect on 1 May 1995, all individual and corporate entrepreneurs (including individual farmers) had to be registered as VAT payers if their turnover in the previous 12 months exceeded LVL 10 000 and were entitled to register if their turnover was more than LVL 7 500. Agriculture co-operatives are free of VAT for services provided to private farms not paying VAT. Private farms not registered as VAT payers are entitled to compensation for VAT paid on inputs at a rate of 15 per cent of the input price without VAT.

g) Land tax

The land tax is based on a points system of land valuation that depends on soil quality as well as on location. The tax for unused agriculture land is double, so the system is intended to stimulate land use. Private farms in Latgale (the less favoured region) and those that started farming under difficult conditions may be exempt from land tax for a maximum period of five years.

The local authorities have the power to reduce land tax further for land users bringing virgin land into cultivation or making substantial investments for land improvement.

h) Property (fixed assets) tax

The property tax is not payable on assets used only in agriculture or on assets used in services provided to agriculture. In other sectors, the rate of property tax depends on the value of the property. Enterprises with property worth less than 1 500 Latis are exempt from property tax.

E. Infrastructure policy

1. Research and development

The agricultural research activities financed by the state, including the research activities meeting the needs of private farmers, are concentrated in the State Scientific Research Institutes of the Ministry of Agriculture, the Latvian University of Agriculture and the Fundamental Research Institutes of the Latvian Academy of Sciences. The main institutions carrying out research in agriculture are:

- Latvian State Research Institute of Agriculture;
- Latvian State Research Institute of Animal Husbandry and Veterinary Science;
- Latvian State Research Institute of Agriculture Engineering;
- Latvian State Institute of Agrarian Economics;
- Latvian University of Agriculture (with seven faculties and several Institutes within the University.

These institutions are mostly funded by the state budget, but some income is earned from commercial contracts for the supply of services, which are mostly provided by large companies rather than individual farmers.

The "Law on Scientific Research" was passed in October 1992, giving private persons and companies the right to undertake scientific research activities and to obtain budgetary funding for them, but they have to compete for research grants with other research bodies.

A Council of Science under the supervision of the Latvian Cabinet was founded in 1991 for the co-ordination of research activities. The Council receives an annual allocation (in 1993 it was 0.73 per cent of the state budget) to finance research projects, including in agriculture.

It should be noted, however, that the Council does not co-ordinate research work financed by individual ministries. The Ministry of Agriculture receives an annual allocation from the state budget to carry out contract research and the projects it considers to be the most urgent.

The Academy of Agriculture and Forestry Science of Latvia was founded at the end of 1992 to co-ordinate and develop scientific research work in agriculture and to establish centres for farmers' educational and advisory services. The Academy members are researchers from the Latvian University of Agriculture and other scientific institutes collaborating on a personal and voluntary basis. The academy is a public, non-profit-making institution.

Under the supervision of the Ministry of Agriculture, there are also 12 selection and experimental stations (including seven selection stations for plant growing that select the main agricultural crops, six experimental stations for animal husbandry and the Baltic machine testing station), as well as the Latvian Centre of Plant Protection and the state scientific enterprise Raziba, involved in increasing soil fertility.

2. *Training and extension*

a) Latvian Agricultural Advisory Centre

The leading advisory service is the Advisory Centre of Agriculture, which was established by the government and is financed by the state budget. It was created following the signing of a Co-operation Agreement between the Latvian Ministry of Agriculture and the Danish Farmers' Union in 1990. The Advisory Centre was opened in September 1992 on the recommendations of a group of Danish researchers working in conjunction with Latvian experts. The Latvian agricultural advisory service consists of the Advisory Centre located in Ozolnieki, 40 km from Riga, 25 district offices and more than 250 local advisors, usually one for two pagasts.

The Advisory Centre provides support to regional advisory offices and local advisors free of charge. The main task of local advisory offices is to provide training for farmers and their families with a view to increasing the profitability of farms and improving farmers' working conditions.

The Advisory services's activities span all administrative levels:

- State level, where it co-ordinates the network of advisory offices, provides information to consultants, exchanges information with research institutions and extension centres in foreign countries, and so on.
- District level, where it sets up and co-ordinates the advisory network in the *pagasts,* organises the training of farmers, provides field advice in the *pagasts,* and holds direct consultations with the farmers.
- *Pagasts* level, where it provides advice to local farmers, informs clients about information sources available, and so on. At present, there are advisers in about 40 per cent of *pagasts.*

Farmers can also get advice from qualified specialists: agronomists, veterinary doctors and accountants working in large corporate farms. In those cases, services are provided at agreed prices. Information is also available from five (weekly or monthly) newspapers or magazines, which offer practical advice to farmers, from surveys of the latest science publications, from the publications of private publishing houses, and from the editorial boards of magazine publishers. The demand for advisory services is greater for market advice (70 per cent) than for technical advice (30 per cent). As the agricultural sector develops, there is a growing demand for economic and farm management advice. In winter, farm accountancy courses are well attended.

The lack of finance limits not only the numbers of advisers available but especially the quality of advisory staff. The current system of agricultural education covers a relatively narrow range of subjects and there is a need for advisers with broader knowledge, especially of business management and farm economics. This problem could be resolved by providing additional training to advisers, although they are being regularly sent abroad for further study. The service's efficiency is also limited by the lack of finance to provide field advisers with transport facilities (cars, fuel, and so on).

b) Agricultural education

The Latvian system of specialised agricultural education consists of 24 professional secondary schools, which teach basic occupational skills to agricultural workers. About 4 500 new pupils per year attend these schools. In addition, 15 agricultural technical colleges provide basic training, taking about 1 250 new pupils annually. These schools and colleges are located throughout the country. They are usually attended by youngsters who have completed nine years' basic education. For those pupils, the courses are for three or four years, and in additional to occupational training, they receive a general secondary education. Older students can enter these schools on leaving a general secondary school, and receive a two-year specialist course in agronomy, animal sciences, agricultural mechanisation or in one of a further 15 specialist subjects. Almost all these schools offer short-term courses (not exceeding one year) to improve the farming skills of persons entering or already involved in farming. There are a total of 1 500 teachers in these secondary schools throughout the country. These 39 rural schools and technical colleges are attached to the Department of Education and Science of the Latvian Ministry of Agriculture and are financed from state and local budgets.

There is only one agricultural university in Latvia – the Latvian University of Agriculture (LUA) in Jelgava, 40 km south of Riga. LUA offers undergraduate and graduate education, research and extension in agriculture, food and forestry in the following subjects: agriculture, economics, veterinary medicine, mechanisation of agriculture, rural engineering, food production and forestry. Over the past five years, LUA has admitted 700-800 students annually to its in-house courses and enrolled 200-400 students for correspondence courses. The LUA statutes state that it is an autonomous educational and scientific institution. Under the new Education Law, students can acquire a higher academic qualification (Bachelor's, Master's degree) and a higher professional qualification (Engineer, Engineering Diploma). International co-operation has been successful during the last two to three years; contacts were first established with Germany and the Nordic countries and each year some 80-100 LUA students and 50-80 teachers follow training or study courses abroad.

3. *Quality standards and domestic sanitary control*

At present, Latvia is going through a transition towards a new system of food and quality control. Participation in different international organisations and institutions is also influencing and easing the process. Latvia is currently a member of the following bodies:

- The European and Mediterranean Plant Protection Organisation (EPO) since 1993;
- An observer of WTO/GATT since 1992, and engaged in the process of membership accession since 1994;
- The European Standards Organisation (CEN);
- The Food and Agriculture Organisation of the United Nations (FAO) and Codex Alimentarius Commission (CAC-Codex), since 1992;
- The World Organisation for Animal Health (OYE) since 1992.

a) The Food Quality Assurance Programme

At present, the Ministry of Economy and other ministries and institutions are working on the ''Quality Assurance National Programme'', which is set up within the framework of the Phare Regional Programme. One of the basic sub-programmes is the Food Quality Assurance Programme.

Under this National Programme, a Food Quality Assurance Programme has been drawn up by the Ministries of Economy, Welfare and Agriculture, and other institutions.

The Programme's objective is to create a system covering the whole agro-food chain (including exports and imports) that ensures nutritional safety, human health and environmental welfare, and stimulates exports as a result of better quality and the certification of goods.

To achieve this objective the following laws and regulations were issued in Latvia:

- The law ''On Protection of Consumer Rights'' was adopted on 28 October 1992. It acted as an ''umbrella law'' after which other acts followed in the area of consumer protection.
- The law ''On Veterinary Medicine'' was adopted on 30 June 1992. It regulates the special area of unprocessed animal products (milk, eggs, honey, etc.). The law specifies that the task of veterinary medicine is to apply veterinary-sanitary expertise to animal products with the main aim of obtaining food and raw materials which are harmless to human health and safety.
- The ''Food Law'' has been prepared and submitted for adoption by parliament in 1995. The Law regulates quality and safety of food raw materials at all stages of the food chain (production, storage, transportation etc.), as well as state supervision of quality control.

Within the framework of the National Programme on Quality Assurance, several regulations have been issued by the Ministry of Welfare, such as those on the ''Mandatory Certification of Foodstuffs, Perfumery and Toys'' (12 April 1994) and the ''Instruction for Obligatory Certification of Food Products, Perfumery, Cosmetics and Toys'' (17 August 1994). Under these regulations, Latvia started to create an independent assessment system for products and services. In addition, regulations on the ''Accrediting Procedure and Certification of Testing and Calibration Laboratories'' were introduced on 23 August 1994.

b) *Import control*

Because Latvia only began to build up a customs system in 1991, the control of imports and exports is inadequate. Currently, the computerisation of customs posts and personnel training is underway. In parallel, a network of health, veterinary and plant quarantine inspectors based at customs posts are controlling cargo. It is also planned to introduce a system of licence registration of foreign trade (import) companies. Some problems have arisen in implementing international directives (EU directives, etc.) and harmonisation standards, FAO, "Codex Alimentarius" and other requirements. Latvia has a very limited possibility to obtain and fully use these documents (problems of translation and interpretation of very specific rules).

4. *Regional and structural policy*

a) *Regional policy*

Regional development is an important area of government policy. The Ministry of Environmental Protection and Regional Development was created in 1993, which took over the existing Regional Environmental Protection Departments that had been set up in 1988-89. Following the reorganisation, these agencies started to deal with regional development as well as the protection of the environment.

The Ministry of Environmental Protection and Regional Development was formed out of the merger of the Committee on Environmental Protection and the Ministry of Architecture and Buildings. It is divided into six departments, one of which is responsible for regional development. Regional development policy concentrated on territorial planning to start with, and only recently has the Regional Development Department started to deal with broader questions of regional development.

Regulation No. 162 passed by the Cabinet on 12 April 1994 called for the Ministry of Environmental Protection and Regional Development to draw up a national programme for rural development in Latvia. A statistical survey of the existing situation in Latvian *pagasts* was produced in 1994. Some 34 thematic maps were drawn to evaluate the potential for developing regions and *pagasts,* which served as the basic concept for the formulation of Latvian rural development policy.

After analysing this information, it was found that regional development could not be related solely to rural development but that a national development programme needed to be drawn up. Called the Latvian National Programme for Regional Development, the conceptual basis for it was laid in 1995, and in September of that year the Cabinet decided on the general framework of its new regional development policy. A regional development law is being drafted and work is going ahead to put flesh on the bones of the National Programme for Regional Development.

b) *Structural policy*

Because of the general lack of credit finance available in the financial markets and the country's very limited budgetary resources, it has not been possible to tackle the real problems of the structural adjustment of Latvian agriculture, including farm modernisation. The few and limited attempts made to provide financial assistance to the emerging individual farms sector have mainly relied on credits from abroad, as described in the section on credit policies. In view of these limited resources, policy has been deliberately targeted at promoting the modernisation of individual farms, including improvements in working practices.

In reality, though, no real programme existed for bringing about the modernisation even of the individual private farming sector. which is essential for an improvement in the sector's overall efficiency. For the future, assistance should be less selective as regards the type of enterprise but very selective as far as the efficiency and market orientation of the recipient farm is concerned.

F. Environmental measures

Before 1988, conflicts of interest between production plans and environmental norms meant the latter were often neglected. In 1988 the State Committee of Environmental Protection and its regional agencies were created. Since 1993, government environmental protection policy has been the responsibility of the Ministry of Environment Protection and Regional Development, working in close co-operation with the Ministry of Agriculture. Work only really started in 1994 on the drafting of environmental protection legislation.

Latvia as an independent country has joined a number of international environmental conventions and treaties. The Latvian parliament ratified the Convention on the Protection of the Marine Environment of the Baltic Sea Area (Helsinki Convention) on 16 March 1994. Like the other signatories, Latvia is obliged to take all appropriate measures to control and minimise land-based pollution of the marine environment in the Baltic Sea Area. Latvia has also signed the Convention On Protection and use of Transboundary Watercourses and International Lakes.

The 1991 "Law on Environmental Protection" is an omnibus environmental protection law that delegates responsibility for environmental protection, natural resource use, environmental impact assessment procedures, standards, permits and public information and sets out goals for the protection of the environment and the rational utilisation of natural resources.

The 1990 "Law on the Taxation of Natural Resources" established imposed charges for the use of natural resources and the release of effluent within standards and provided for sanctions against those who exceeded permitted levels. Normal tax revenues are shared, with 25 per cent going to the state budget and 75 per cent to local government budgets. Tax revenues for discharges in excess of the prescribed limits are paid into the Environmental Protection Fund, which also collects fines that are used by national and local governments to finance a wide range of activities.

The "Law on Land Use and Land Improvement", passed in 1991, lays down the basic principles for rational land use and protection. The "Law on Plant Protection", passed by parliament in 1995 governs the use of pesticides in agriculture, including their transportation, storage and application. Taking into consideration Latvia's possible accession to the EU, further work on the humanisation of legislation and standardisation is going ahead.

The problems of enforcing environmental protection laws and especially former USSR regulations that are still in force have become increasingly difficult as land and inland waters have been returned to former owners and development pressures arise between environmental agencies and the reinstalled landowners. The Ministry of Environmental Protection and Regional Development, in conjunction with other ministries, drew up guidelines for a National Environmental Policy for the next 20 to 25 years. These guidelines were developed into the National Environmental Policy Plan, already approved by the Cabinet in April 1995, and the National Environmental Action Programme that is being formulated and is expected to be approved by the Cabinet and parliament (*Saeima*).

G. Social measures

The retirement age is fixed at 55 for women and 60 for men. Before 1990, two types of pensions existed:

- State pensions paid out of the state social insurance budget.
- Collective farm pensions paid out of centralised collective farm funds. Pensions from collective farm funds were paid only to those who were members of the collective farms at the time of retirement.

In 1988, the pensions for collective farmers amounted to about 30 per cent of average wages and state pensions to about 38 per cent.

A unified social insurance system financed by the state budget was created in 1990, since the state budget is the sole source of funds for pensions. The value of the pension depends on the average salary paid within the last five years of employment subject to the person having worked a required number of years.

There is a difference in the rate of the social tax for enterprises in agriculture, which pay only half the standard rate of social tax (see section on tax policy). When the reform process started and inflation was very high, the government fixed equal pensions for everybody and pensions were paid independently of the number of years employed. Today, the social tax funds the state social insurance budget and employers cannot set aside any additional funds for pensions. Special pension funds may be created in the future, in which employers will be able to deposit pension funds contributions. Discussions have taken place on introducing a pension self-insurance system and gradually increasing the retirement age to 60 and 65 years. Given that agriculture enterprises are exempt from the social tax, there are no other specific social measures for agriculture.

The unemployment problem has been a major cause for concern since the beginning of the reform process. Unemployment benefits are equal for everybody and are paid from the state social insurance budget. As a rule, unemployment rates are much higher in rural areas than in the cities. Existing legislation is unclear about the conditions for registering as unemployed as regards the rural population working on private self-subsistence plots with no additional sources of income.

H. Consumer measures

During the Soviet period, the regime continuously tried to keep retail food prices well below the rising costs of food production. To keep food prices low, higher subsidies had to be paid at the wholesale level to processing enterprises, although the benefit of these subsidies went to the consumer.

This policy and related measures were abolished in December 1991, when the Government decided to introduce a free price policy throughout the food chain. Later on, the so-called ''ration coupons'' system, giving each Latvian citizen the option of buying a certain amount of scarce agricultural and food commodities at a fixed state price, was also abolished. Until July 1994, a reduced rate of turnover tax was payable on basic food products, but with the introduction of a unified rate of 18 per cent, that indirect support for food consumers was ended. Since then, no further consumer measures have been introduced; the only policy promoting consumers' interests was the tightening of the legislation governing food quality and food safety.