

### **III. The Impact and Consequences of the Future EU Accession of Macedonia for the Agricultural Sector**

**The Influence and Consequences on the Agrar Sector in  
Macedonia as a Result of its Future Entrance in the European  
Union**

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## **Possible Effects from the EU Membership on Macedonian Agriculture and Problems Connected with this Area**

Referring to trade exchange, introducing free trade between EU and Macedonia represents a significant step towards the improvement of the approach of our products. Until the year 2000, more than 80% of Macedonian export entered the European market under free regime. In June 2000 the European Committee proposed an increase of the free approach. The rest of the customs restraints were removed on December 1<sup>st</sup>, 2000.

By this, Macedonian economy gained an opportunity to use the comparative advantages of our country completely. The basis of the Macedonian economy consists of labor-intensive branches such as: food-processing industry and production of beverages, leather and textile industry, chemical, pharmaceutical and tobacco industry. If we take into consideration that all the countries in Central and Eastern Europe as well as all our neighbors on the Balkans have the same branch structure, with mostly traditional activities, it will not be difficult to reach the conclusion that RMacedonia is going to have a great number of competitors on the enlarged European market. What is more important is that all the above-mentioned competitors have been present on that market in a longer period of time and they have already taken the important strategic market segments. What is left for Macedonia is to fight for its position on this market primarily by gradual placement of its products on the market of the former Yugoslav federation. By renewal of the trade connections with the former republics, the primary products with a low level of processing which were used for raw materials and half-products, will find their way to the market.

## **Material and Work Methods**

The complexity and the difficulty of the material taken into consideration for processing, obliges a use of proper econometrical methods such as: observation method, analysis method, index method, comparative method as well as other methods which will contribute to discovery of the most important components of the Macedonian agriculture situation and, to quantify the qualitative figures on the basis of subject research.

Methodological applications of certain econometrical methods are explained in details in the corresponding chapters, which are subject to discussion. The following sources have been used for a complete study of the problem connected with the subject research: existing publications and other information that consider agriculture as an economical branch in RMacedonia. Statistical data from the Statistical Bureau of the Republic were also used, as well as scientific literature, which is listed at the end of this text.

## Theoretical Background

### What do we mean by market generally?

**Market** represents a shape of products and services exchange through money, regular relationship between supply and demand, and a place where the price is formed. On the side of the supply there are the sellers, who provide satisfaction of specific or common needs by their product or service; on the side of the demand there are the buyers, who, being the carriers of certain financial means transform their needs into an effective market force. The term market is very complex itself. It is often used in general terms as a whole of exchange acts among economical subjects within the society, where the division of the labor is done, besides, a market may be defined spatially according to the scope width (local, national and world).

### What is World Market?

The sum of all national markets, i.e. the total of all foreign trade relations in the world represents the world market. The world market includes exchange of goods and money among all the countries, which is considered world export, i.e. world import, by both quantitative and qualitative figures during a calendar year. The world market might be considered also according to the assortment of the goods exchange, the spatial location of the continents or according to international integration groups.

World market is interesting from the aspect of establishing and following of the directions and scope of the world circulation of agriculture and agro-industrial products, especially by types and groups of these products. The importance of establishment of these figures and relations is within the possibility of determining the level of the mutual dependence of the world countries in terms of the possible fund sources for agriculture products, at present development conditions and divisions of the world.

### What is Price?

An expression of a product or a service value declared in money is called a price. The theories of the prices are often divided into two groups: analytical and normative. The first ones consider the issues of what a price is, what regulates their fluctuation and similar issues, while the second ones give answers to what kinds of prices should be established. Occasionally, both approaches – the analytical and the normative one – can be found in a same theory.

### Market Price

**Market price** is a price by which a certain product is sold or bought, and on the market it is formed as a result of the supply and demand relations. It is an

expression of the social-economical relation between the sellers and the buyers in a shape of exchange for money. When the supply and demand is balanced the market price reflects the socially needed work time, which is required for the production of a certain product. According to the supply and demand changes, the market price oscillates around its equilibrium point – the market value of the simple goods production and the prices of the production in a developed capitalistic economy. When the supply exceeds the demand, the market price decreases under the equilibrium price (value), which has an impact on the supply decrease and demand increase. On the contrary, if the market price increases above the value, the supply becomes stronger while the demand decreases. This process, which reflects the social shape of the influence of the value regulation, takes place with a tendency for the market relations to become balanced and for the market price of the goods to get stabile at the point where the supply volume equals the demand volume. At that point the market price is equal to the equilibrium price. Goods manufacturers whose individual value is higher than the market price will not be able to get an equivalent for their labor on the market and they can even work with certain loss. On the other hand, the manufacturers, whose products have lower individual value than the market prices, will make an extra profit.

### **What are the Possible Expenses?**

The expenses in the most general sense represent a sum of money paid or given for a special product or service (a sum of money really paid or calculated for buying goods and services or a sum which is spent internally for production of goods and services).

The movement of certain expenses categories depending on the production volume dynamics is the basis for expenses classification: permanent and variable, average and marginal, direct and common. From the perspective of the reproduction process phase in the enterprise, the expenses can be classified in the following way: reproduction expenses and circulation expenses. Furthermore, there are: economy propaganda expenses, production expenses, circulation expenses, substitution expenses, life expenses etc.

### **What is the Agrar Policy of RMacedonia?**

We can say that Macedonia is mostly an agrarian country. Facing quantitative limits, meaning quotas for the main agriculture products, the possibility for export was on a minimum level. Therefore, after the establishment of free trade with the EU, now Macedonia will have to pay more attention to this factor. The comparative advantages of RMacedonia lie exactly in the agriculture and more specifically in the production of healthy food, production of beverages and tobacco processing. Wide spectrum of fruit, vegetables, cereals, dairy and meat products produced in this area offer great export possibilities. However, further reforms in the agriculture sector should be made such as finalization of the privatization process of the agro-combinats, modernization and reconstruction of

the farms by putting an input of modern technology for soil processing, modernization of the veterinary and phytosanitary laboratories, as well as training and courses for the individual producers for healthy food growth and production. These reforms aim at a successful development of the export platform, which will comply with the European quality standards.

A significant precondition for the development of our economy is the attraction of foreign direct investments. The foreign capital influx will depend on the conducting and finalizing the market reforms. Because of the territorial size of our market, RMacedonia cannot attract market-oriented investments. The only optimal platform is the export one. Thus, RMacedonia could become the supply center primarily in the Balkan region, then in the Central-Eastern region and finally the European market. In order to achieve such an export competitive situation, attraction of foreign direct investments is needed, which will provide transfers of contemporary labor-intensive technologies, by which new jobs for the unemployed and unqualified personnel will be opened. Following the example of the Asian tigers, providing investments in high-technological production and service activities would not be incorrect since Macedonian economy has a potential of young highly qualified workers especially in the area of computer science.

By this, the positive multiplier effect of the foreign direct investments will contribute to the development of the secondary activities and services network, decrease of the unemployment (the rate of which is around 30%), improvement of the bank sector solvency, as well as increase of the international credibility of the country as a whole.

## **Basic Elements of the CAP**

The basic aims of the Common Agricultural Policy are:

- Guaranty for secure food supply with stable and reasonable prices;
- Productivity improvement through technical progress and rational production, and
- Providing good life standard for the farmers.

In order to achieve the above-mentioned objectives, EU has taken the necessary measures, by which:

- Mutual market organization for agricultural products within the frames of all significant agricultural branches has been established,
- A system of common prices has been introduced, production and selling aid, as well as providing storage of the production; and
- A mechanism for export and import stabilization has been provided.

Long-lasting and hard discussions about the level of price support and protection reoccur every year, and after the launching of the green paper by the European Committee (1985), a wide debate was initiated for the future of the

European agriculture. The Committee accepted the results of those debates, which were in the form of memorandums and briefly add up to:

- A request for a progressive decrease in the production in the surplus sectors, price policy which will reflect on the market demand;
- Taking into consideration the income problems in small family farms in a more effective and systematic way;
- Support of the agriculture in areas where it is necessary because of the regional development, by a simultaneous support of the social balance and environment protection; as well as
- Promotion of an increased conscience level in farmers in terms of the problems for the environment protection.

The idea and the crucial point of the mentioned directives necessarily determined the steps in a direction of a market organization reform, which is one of the essential conclusions of the European Council, passed in 1988.

The basic mutual aim of the reform is: decrease of the price when the quantities of a certain product produced extend the deduced threshold, by an increase of the consumers share in the expenses financing, for instance – cereals.

This kind of a market organization, based primarily on the price policy, is accompanied by certain measures, which have double objective:

- To decrease the volume of the production by revoking certain seed surfaces, extending the production, production converting as well as implementing a so called pre-pension aid which is bound to non-usage of the land; and
- To moderate the income effects in the majority of vulnerable (small) farmers because of the decrease of the prices and increase of the co-responsibility. Help schemes for the small producers and decrease of the co-responsibility in the main market organization (for milk and cereals) tended towards fulfilment of their interest.

## **Possible Adjustments of the Macedonian Agrar Policy to the CAP**

Before starting the process of adjustment of the agrar policy in accordance with the agriculture subsidies in RMacedonia to WTO and EU, we should consider the existence of tolerance for application of subsidies and its level according to the WTO rules. Referring to a survey by USAID, it is known that the subsidiaries in the agriculture are not invalidated but they should be decreased in the following way:

- The developing countries should decrease the subsidy level in agriculture by 13.3% with reference to the basis period 1986-1988 in the developed countries, to the level of PES (production equivalent of subsidies) in a period of 10 years (meaning until 2004). The developed countries should do it to 20% in 6 years.

So, according to the Agreement, developed countries (including the ones in EU), should have completed the decrease up to year 2001, and our country, as a developing one, should complete the planned decrease, of both direct or export subsidies until the end of 2004. According to this, RMacedonia can have subsidies in agriculture even more than 13.3% of the developed countries average in the period of 1986-1988 until 2004, and after that the level should be maintained. However, in 1997 direct subsidies were revoked. Also, referring to the decrease of export stimulation, it was not necessary for them to be revoked, but they should have been decreasing until 2004, and then kept at the necessary level. Instead, in 1997 we revoked the export stimulations. So, while developed countries are using the Agreement rules for a gradual decrease of agriculture subsidies, and not only them but also developing countries such as Slovenia and Croatia were doing it. Macedonia, causing damage to its economical interests for the agro-complex development during the transitional period, abandoned the necessary subsidies for stimulation of the producers for a greater and more profitable agricultural production.

Abandoning the subsidies in agriculture in Macedonia is a serious problem, since in the current middle term; GDP in agriculture has an unsatisfactory average rate of 0.3%. Thus, in order to revitalize the agriculture sector and the villages, along many other issues, the financial stimulation for the producers in the agro-complex has to be returned to a satisfactory level through forming a special fund for that purpose, which was done in 2001. For the future, through the fund, the model for the agrar reform implemented in EU can be applied.

Anyway, providing proper credit lines and investment means should be of greatest importance, but if a profitable surrounding is not secured at least for the better producers in terms of placement and market, they will soon transform into debts and their lack of interest for further development.

### **What do we Know about Macedonian Agriculture and Agrar Policy?**

The strategy of the agrar policy in a country, including ours, should provide a desired possible strategic development of the agro-complex in that country. However, after gaining its independence, RMacedonia started implementing a restrictive policy in terms of various subsidies as stimulating measures for a more rapid development of the agro-complex. The main reason for this were the bad economical conditions in the country's economy in general, but also the act of acceptance of unilateral suggestions from certain IMF and WB experts, who permanently suggested that the state should release itself as soon as possible from any kind of subsidies referring to the future development of the agriculture. Consequently, a short analysis for the conditions of the agrar policy in RMacedonia, the adjustment to the WTO rules and the reforms implemented in EU is worth considering.

The agrar policy and the village in Macedonia should encompass the following segments: a) macro economical frames for development of the agriculture; b) land reforms and reorganization of the agrar structure (agriculture economies); c)

competitive and efficient farm work and processing and service activities for the agriculture; d) rural financing, and e) institutional frame for support of the agriculture development.

### *Macro economical frames for development of the agriculture*

Within the macro economical frames for development of the agriculture, questions such as a) price subsidies b) infrastructure development projects and c) trade policy have a significant place.

Table 1. *Subsidies for agriculture in the budget of MAFWE (millions Denars) (Source: Budgets of RM, Official Gazette 1994-2001, Skopje)*

Type of subsidies	1994	1995	1996	1997	1998	1999	2000	2001
Money regress for seeds	177	178	161	0	0	0	0	0
Money regress for credit lines interest	954	149	0	0	0	0	0	0
Bonuses	889	740	352	71	0	0	0	0
Development initiation program	75	92	210	361	233	244	229	214
Village revitalization program	0	15	15	15	20	20	20	25
Investments program	0	0	0	0	19	48	82	132
Total subsidies in the MAFWE budget	2095	1174	738	447	272	312	331	606
Index 1994 = 100	100	56	35	21	13	15	16	29
Share of the RM budget, %	3.2	1.7	1.1	0.7	0.4	0.4	0.5	1.0
Share of GNP, %	1.4	0.7	0.4	0.2	0.1	0.1	-	-

### Price subsidies and capital transfers

The main mechanisms and measures of the agrar policy for support of the agriculture development are various subsidies categories (financial stimulations) by the state such as:

- a) direct price subsidies for significant agriculture products;
- b) credit line policy, subsidies on the inputs and investment support in the agriculture;
- c) export stimulations, duty expenses and levies in the international trade.

The Ministry of Agriculture, Forestry and Water Economy has the main responsibilities in terms of direct price subsidies and the subsidies on the inputs in agriculture, for which purpose, the Ministry gains special budget means by the state. The Ministry of Economy and the Ministry of External affairs are liable for the subsidies categories b) and c). The Ministry of Finance is the main regulator of all the subsidies categories in agriculture.

### Direct price subsidies

As it is shown in Table 1, the subsidies for agriculture in the MAFWE budget since 1994 until now, have decreased completely (being 3.2% firstly and then

0.4% in 2000). In 2001, the share is increased to 1%, which is due to bigger capital transfers of the Government for used credit lines of structural agriculture development projects. Practically, direct price subsidies in this period have stopped and remain only as means for every year program for initiation of agriculture development.

A program, which is very important, but refers mainly to activities support of the Agency for promotion of individual producers on the basis of giving financial support for purchase of seed materials, reoning etc. in the vegetable growing branch, for production of seeding material in fruit growing and viniculture as well in the livestock breeding for purchase of male breeding stock, artificial seeding process, implementing individual book keeping etc, with a total input of around €4 million. So for example, in 1999 total budget amount for subsidies in agriculture through MAFWE was € 5.14 million. It is an amount that represents only 0.4 % of the state budget or 0.1% of GDP. If we compare this fact with the intervention subsidies fund in agriculture in Slovenia, which was constantly rising and in 1997 reached the level of over €200 million (3.3% of the state budget), we can see how great our negligence for financial initiation of the producers for the development of the agriculture in Macedonia is.

#### The situation with the production prices

The comparison of domestic production prices of the important agriculture products (expressed in €) with the ones in Slovenia, shown in a percentage relation with the prices of EU and realized prices in import and export, is very interesting.

Table 2. *Index of domestic production prices in Slovenia in relation with the ones in EU – 1997 (Source: Official Gazette of RM from 1998; EU 1998 Report, Brussels; CEEC-Slovenia-European Commission, 1998)*

Products	Domestic production prices % of		Slovenias prices as % of EU-prices
	Export-import prices	EU-prices	
Wheat	99	105	146
Barley	61	98	104
Corn	79	103	79
Rice	70	130	-
Sugar beet in sugar	68	48	97
Sunflower in eating oil	73	113	-
Tomatoes	129	60	87
Apples	77	37	68
Table grapes	93	29	-
Beef/Veal meat	99	104	99
Pork	66	116	113
Lamb meat	77	59	-
Eggs	83	115	-
Cow milk	33	29	90
Wine	85	55	-
Tobacco in tonga	42	59	-

It is certain that data from one year cannot give the real picture, but it shows certain orientation that domestic production prices of only a few products are insignificantly above those in EU (rice, sunflower oil, pork meat and eggs). One

part of the prices is very close to those in EU (barley, corn and beef meat) and the rest of the prices are significantly below the ones in EU.

According to the above-mentioned and the comparison with the production prices in Slovenia, it can be concluded that domestic producers show competitive agriculture production both in comparison with the ones in EU and Slovenia, and even in comparison with the realized prices in import and export. However, the domestic production price is low, which brings low income. It shows that the state as an undeveloped one and in a period of transition has to use protection and initiation measures for development of agriculture production in a certain period of time.

#### External trade policy and measures

In the market policy for outer trade our country used a lot of means for export stimulations for export oriented agriculture products (export levies, when the world price is lower than the domestic one), which were stopped in 1997. However, the usage of relatively high import (customs) fees continued, as a protection measure for the domestic agriculture products when imported.

Table 3. *Import and import customs fees for the import of agriculture products (Source: A report by Customs Administration, Skopje)*

	1998	1999	1999/1998
Total import, million Denars	19 961	15 926	80
Total customs expenses, million Denars	6 205	6 044	97
% of total export customs expense	35.00	38.00	-
Basic customs, %	9.65	11.96	99
Special customs, %	15.83	17.12	102
Levies, %	3.52	4.16	111
Tax, %	3.20	3.65	105
Excise, %	1.80	0.11	5
Book keeping, %	1.00	1.00	100

Table 4. *Macedonian, Slovenian and GATT import tariffs (rates) in percent (Source: Official Gazette no. 15/01; CEEC - Slovenia 1998, European Commission)*

Products	Macedonia 2001	Slovenia 1997	GATT 2000
Wheat	20	5	5
Flour	25	-	-
Corn	2	11	8
Rice	60	-	-
Raw material for cooking oil	25	-	-
Sugar raw material	2	17	12
Tomatoes	40	-	-
Apples	60	-	-
Table grapes	60	-	-
Beef/Veal	18	12	9
Lamb	40	-	-
Pork	20	14	11
Chicken meat	20	14	11
White cheese and cheese	35	-	-
Eggs	40	6	5
Wine	50	23	17
Tobacco oriental	30	-	-

The import customs fees represent 35% to 38% of the total amount of agriculture and agro-industrial products import. Practically, the main customs rate was from 25% to 30%, then the levies from 3.5% to 4.2% and the rest were tax and administrative expenses for customs process, and the excises had an insignificant part.

The levies are an ad hoc established variable import expense because of the introduction of the import (world) price on a protective domestic price level. Laws determined the main customs rates.

As it is well known, GATT enforces low import tariff rates and it can be seen that Slovenia is adjusting great deal to those rates. At the same time Macedonian tariff rates are in great discrepancy compared with the ones given by GATT, but some of them will be further adjusted.

### *Some basic facts about Macedonian agriculture*

#### Land policy and restructuring of the agrar structure

At present, the land reform and the process of restructuring of the agrar structure in our country, is conducted through the Law on agriculture land (1998) and the Law on transformation of agricultural organizations that use the agriculture land (1996).

According to the law on agriculture land, two different forms of agriculture economies characterize the condition of the agricultural sector in Macedonia: small individual (family) agriculture economies, which use their own land and large agriculture organizations (enterprises and cooperatives), which are almost privatized and transformed.

#### Individual agriculture economies

The individual agriculture economies officially have a disposal of 460 000 ha, meaning that they participate with 73% of the total arable land in the state, and their average size is 2.58 ha. However, if we take into consideration the data from the latest census in 1994, the same 178 000 individual agriculture economies stated that they used only 229 000 ha of arable land, which means that their average size is 1.29 ha. The conclusion of this is that they have a disposal of it (according to the cadastre), but probably they use only around 50% of the arable land. This is a question, which should be answered by the State Statistics Bureau.

On the other hand, the number of individual agricultural economies itself can be questioned, because if we make changes according to the EUROSTAT standards (as a result of stricter criteria) their number will decrease (for instance, in Slovenia it was 40% of the number in former SFRJ). Accordingly, if this happens in our country as well, instead of 178 000, we will have 71 000 economies with an average size of 3.23 ha used arable land (which means that around 100 families are not agriculture economies). This issue should also be solved by the latest census done by the State Statistics Bureau.

According to the Census in 1994, the individual agriculture economies participate with 18.8%, the combined ones with 36.3%, non-agriculture ones with 36.1%, and the elderly households with 8.8% of the total number of households.

Although there is an opportunity for the individual farmers to rent land from the agriculture enterprises (according to the Law, 15% of the arable land is already granted), the farmers do not show any interest to rent it because of the low results in the production, they cannot pay the rent.

#### Agriculture enterprises

There are various unadjusted statistical data referring to the participation of the agriculture enterprises in the usage of the agriculture land. Officially, they used more than 600 000 ha agriculture land, but according to the statistical previews, they use only 167 000 ha (the rest of the land are pastures governed by the Public Enterprise for Pastures).

According to the data by the Privatization Agency (March 1999), 243 agriculture enterprises are registered, 145 of which were privatized, and the rest of them are in a process of insolvency or bankruptcy.

By comparison of the data from table 5, it can be seen that the agriculture enterprises before the privatization (1997), are shown statistically with a very large used surface (615 000 ha), against 165 000 ha (only for the 35 agro-combinats) according to the research. By the transformation, those 35 agro-combinats were transformed into 120 companies as complete agricultural enterprises with an average size of 1 376 ha, and 57 companies as food-processing and service enterprises, 9 of which are wine cellars, 9 are dairies, 6 are slaughter-houses, 2 refrigerating warehouses, 5 are canning factories and processing enterprises, 2 factories for cattle food, 11 service companies within trade enterprises, 6 are for cooperation, 3 for catering, 3 for accounting and 1 hydro-melioration system. To sum up, the new system of transition brought disintegration.

Table 5. *The condition of the property structure before and after privatization*

Condition according to SY RM/1999 Size for the year 1999			Condition according to the research 35 Agro-combinats 1997 after privatization 99			
Ha	No.	ha/no.	No.	Ha/no.	No.	Ha/no.
< 500	69	114	7	251	7	251
500-1000	24	742	6	800	16	480
1000-2000	24	1 572	7	1 520	20	820
2500-5000	16	3 527	4	3 480	21	927
> 5000	24	20 620	11	12 170	104	1 288
Total	157	3 916	35	4 718	168	982
Total agriculture surface in ha		614 811		165 133		165 133
Smaller agriculture enterprises			75		75	-
Total number	157		110		243	-

## Adjustment to the existing CAP

### *Scenario 1: Stabilization and Association Agreement with EU*

From October 2000, the following has been planned by the enforcement of the Stabilization and Association Agreement between RM and EU:

- The Union will revoke the customs expenses for agriculture products import originated from RMacedonia, except for the ones with tariff marks for: live cattle, fresh and frozen beef and wine (from the combined nomenclature according to the Official Gazette. of RM no. 15/01). The customs expenses for fish and fish products will be revoked.
- The Union will establish a customs expense, 20% within the tariff quote 1670 tones baby beef for import originated from RMacedonia with a specially defined tariff mark (Annex II).
- RMacedonia will revoke the customs expenses for import of agriculture products originated from the EU for: certain agriculture products, stated in Annex IV (a); (b) certain, stated in Annex IV (b), within the frames of planned quotas for each product; c) RM will revoke the expenses which have the same effect as the customs ones, i.e. it will reduce them for fish and fish products originated from the EU for 50% of the most privileged nation (Annex IV (c); and d) with a special protocol 3, in the Annexes I and II, all the trade arrangements for agriculture products processing for which all the customs expenses are revoked, are stated.

So, by the Stabilization and Association Agreement with EU, in terms of agriculture and fishery trade, obligational relations are planned only in the case of the import customs expenses regime on three levels: a) import of a group of products without customs expenses (the ones in Annexes I and II); b) a group of products with progressive decrease of import customs rates with reference to the most privileged nation (those in Annex II) and c) a group of products with a progressive increase of quotas and decrease of the percentage of customs rates in the following three years (those in Annex IV b and c).

Referring to the abovementioned relations, in *Table 6* a review in terms of the expected changes in the important agriculture products in the following 3 years for the RMacedonia is given.

So, according to the import customs rates, the Agreement does not affect the planned ones in Official Gazette no. 15/01 for: wheat, wheat flour, rice, tomatoes, apples, grapes, beef meat, cow milk and eggs. While for the import of: corn, raw oil, raw sugar (sugar), pork and chicken meat and milk powder, customs rates above certain tariff quotas for the following three years are imposed. Finally, the customs rate for cheese and cream import is planned in percentage of the customs for the most privileged nation and for the wine according to a special treaty and for oriental tobacco, free import, without customs fees.

The state responsible bodies are committed to follow the market neatly and to detect the serious disturbances on time in any sector of the importing party and to take corresponding measures such as: revoking, decreasing or increasing of the customs rates, through the Council or the Committee for Stabilization and Association.

Table 6. *Import expenses for the important agriculture products according to the Agreement with EU (Source: Galev, T. & Dimitrievski, D. 2001. The agricultural policy in the Republic of Macedonia and its adjustment to the World Trade Organization and SAR of the European Union)*

Products	Level of customs	2001	2002	2003
Wheat	According to Official Gazette	20%		
Flour	According to Official Gazette	25%		
Corn	Rate > quota tons	90>20 000	80>20 000	70>20 000
Rise	According to Official Gazette	60%		
Raw oil	Rate > quota tons	90>5 000	80>10 000	70>15 000
Raw sugar and sugar	Rate > quota tons	90>5 000	80>10 000	70>15 000
Tomatoes and peppers	According to Official Gazette	40%		
Apples	According to Official Gazette	60%		
Table grapes	According to Official Gazette	60%		
Beef	According to Official Gazette	18%		
Lamb meat	Without quotas (for export)			
Pork	Rate > quota tons	90>2 000	80>2 000	70>2 000
Chicken meat	Rate > quota tons	90>1 500	80>2 000	70>3 000
Cow milk	According to Official Gazette	25%		
Milk powder	Rate>quota tons	90>200	80>300	70>400
Cheese and cheese cream	% of the most privileged nation	80%	65%	50%
Eggs	According to Official Gazette	40%		
Wine	Special treaty			
Oriental tobacco	Without customs (export)			

## Scenario 2: Free trade with agriculture products

Agreements for free trade with other countries. Besides the Agreement with EU, Macedonia has made Agreements for free trade with Slovenia (1996), SRJugoslavia (1996), Croatia (1997), Bulgaria, Switzerland, Norway and Iceland. At present negotiations are going on for free trade agreements with Albania, Bosnia and Herzegovina, Romania and Ukraine. Also, Macedonia is negotiating for associative membership in CEFTA. By these agreements, the free trade for agriculture products is significantly enlarged, both by volume and without customs fees.

By the above-mentioned free import quotas (without customs fees) for significant agriculture products originated from former Yugoslavia, it seems that on one hand Macedonia satisfies its needs, and on the other hand, it provides large export into these countries. However, when looking at the trade exchange it can be

noticed that there are some problems in terms of the fulfilment of the planned quotas for import and export of certain products, which is the reason why the export from Macedonia is not reciprocal with the other countries and vice versa, especially with Slovenia and Croatia. That is why attention should be paid to the gravity both on the agreeing and on the conducting of the Agreements for free trade with any country, in terms of more precise planning of the export-import tariff quotas size and the possibility for their fulfilment by any of the agreement parties.

Table 7. *Tariff quotas for free export of certain agriculture products from Macedonia, Slovenia, SRJ and Croatia (Source: Free Trade Agreements Official Gazette no. 48/96, no.59/96 and no.28/97)*

From Macedonia to Slovenia		From Slovenia to Macedonia		From Macedonia to Croatia		From Croatia to Macedonia	
Product	Quotas t.	Product	Quotas t.	Product	Quotas t.	Product	Quotas t.
Lamb	100	Poultry	3 950	Lamb	800	Poultry	1 200
Tomatoes	2 000	Pork	100	Tomatoes	4 000	Fresh fish	250
Peppers	2 000	Milk	3 000	Peppers	3 500	Milk	600
Grapes	1 000	Milk powder	50	Grapes	8 000	Yogurt	150
Wine	22 000	Cheese	50	Apples	1 000	Cheese	300
Tobacco	1 500	Butter	50	Rise	3 000	Tobacco	2 500
				Wine	4 000		
				Tobacco	2 500		
From SRJ to Macedonia							
Product	Quotas t.						
Wheat	100 000						
Wheat flour	10 000						
Oil (sunflower)	500						
Sugar	700						
Life cattle number	4 600						
Pork	1 000						
Milk and cream	750						
Cheese and cream cheese	100						

By conducting the free trade agreements, both the one with the EU and the ones with the other countries, RMacedonia in future will significantly revoke and reduce the import customs expenses, especially for the significant agriculture products, and the domestic producers will feel the disloyal competence of the free import even more. Because of that, we can freely say that the bigger the globalization of the trade exchange is (which is an inevitable process), the greater the need of the domestic producers for more effective direct financial initiations and protective measures for securing a profitable market for their products will be.

### **Scenario 3: Free trade plus direct pay of the local and regional activities regarding the agriculture**

The current situation imposes the need to redefine the protection measures. The agriculture preferences, showed through classical customs, shipments (quotas) the normative regulations for the quality and through the other performances of the goods, of the export rates and administrative measures, do not integrate fully the Macedonian agriculture. The overall quantity of the few important products that are intended for export, do not fit in the contingents of the world trade economy. The overproduction of the Macedonian region of: lamb, vegetables, fruit (apples), wine, tobacco and in some years rice, find their realization on the deficient European market very hard. So, Germany feels a need to import vegetables, fruit, wine, veal and pork, then on the Italian and Greek market there is a shortage of yearling beef, veal, lamb and pork, while the Netherlands, Luxembourg, Ireland and Denmark have a shortage of wine, vegetables and fruit.

Increase of the export orientation, of the other surplus products, can be achieved if positive elements for urging high quality agricultural production, according to the taste of the customers are implemented in the agricultural policy. First of all it is about the export subsidies, about the coordination of our standards with the standards and regulations of the EU and other parts of the world and for coordination of the foreign trade regime and in the conditions for import of raw materials and semi-finished materials.

The export subsidies should involve, above all, the products from the higher phases of processing. The coordination of the standards is necessary in order to remove the technical obstacles in the turnover and in order to adjust the unified interior market of the EU.

The arrangement of the subsidies in the export depends on the material capabilities of the country. It would be ideal if Macedonia could make subsidies for the whole agricultural production, which will be exported according to the world price lower than the domestic production price. The list of products that could be exported is very wide, and at the same time they have low labor productivity, high costs and high production price. High participation is needed to make them competitive on the international market that is to say to coordinate the domestic price with the low world price. The use of the subsidies in the export of the agricultural products enables equality, reality and economy, only if the state financial reserves are on a satisfactory level and if the overproduction threatens the standard of the producer, the economy and political system of the country.

Macedonia, as a country with limited financial capital, can afford subsidies directly in the process of the agricultural production, through premium, bonus and compensation.

It would be best if the participation of the export elements can be done by subsidies for the transportation and energy costs, by lowering the tax rates and most of all by approving consumer credit lines for the country, which is importing Macedonian agricultural products.

# What is best for Macedonia According to

## Basic strategies, regarding

### *Acceleration or deceleration of migration from rural to urban areas*

The Macedonian villages cover 86.7% of the national area and 40.2% people of the whole population live in them. The agriculture is the main economy activity of the rural population, and the households that have individual agricultural enterprises have an important place in the agricultural structure (73% arable soil, 90% cattle, 96% tractors), which entitles them with an important role in the production results.

All in all, the village in RMacedonia is systematically neglected in terms of demographical, economical and social aspect. The number of rural communities that have good development is very small.

Nearly 3/5 (60%) of the Macedonian village is infected by depopulation especially the sensitive regions of the country such as the hill and mountain regions and the compact backward regions.

The insecurity of the rural environment: the permanent structural changes of the soil (partitioning of the soil), difficulty in reaching the educational and health institutions, absence of employment outside the agriculture and the low quality of the infrastructure, are the basic factors that push the population out of the rural communities.

The current economic and social problems of the village are a result not only of the economic transition, although it is one of the factors with negative impact, but also of the inherited level of economic and social development from the previous years. Those problems were present even before the transition started, and they are still present in the village.

The rural population in R. Macedonia is faced with: low income and unsolved basic infrastructure needs of the rural settlements. The survey of the Republic institute for statistics shows that only in 30% of the agricultural households the income hardly satisfies their needs. The lack of satisfaction of the annual incomes from the agriculture is a result of: small and partitioned land assets (2 ha on average), obsolescent technology, low rank cultivation of the land, unorganized market approach etc.

The factors in R. Macedonia that contribute to the greatest extent to the insecurity of the rural population are:

- the unsolved basic infrastructure needs of the rural environment (road, regular bus, supply with the basic products, enough healthy drinking water, sewerage system etc).
- difficulty to reach the educational institutions especially for the people who live in the hills and mountain regions;

- difficulty to reach the market and the market information which disables the small farmers to make better prices for their products and lower prices for the raw materials;
- inaccessibility to the basic health services, including the primary health services.

According to the Law for pension and disability insurance only the farmers who are obliged to pay income tax from the agricultural activities, have the right to pay contribution for pension and disability and they are entitled to a pension. The average pension of the farmers is 30% lower than the average pension in Macedonia, while the retired farmers according to the Law on age insurance of farmers, have a pension lower than 50%.

The stagnation of the economical development of the rural area increased the poverty and worsened the social security of the rural population. The transition towards market economy, the privatization, caused considerable decrease of the real standard of living of the rural population, which had a suitable impact on the level of social development. As a result of the high increase of the living expenses and the decreased purchase power of the population, increase in the expenses for food, housing, heating, lighting, health and hygiene is noticed. The households are forced to reduce the expenses for clothes, shoes, furniture, as well as for saving.

#### *A new approach towards rural development*

The integral approach of the rural community, meaning the overall economy, social and cultural progress of the rural space and community has proved to be a successful model for revival and progress of the rural communities in Western Europe. In terms of the strategy for spatial development, the integral rural development seeks urbanization of the rural communities. And that is a transition of the concept for development of the urban centers to a concept for development of the space, in order to reduce the regional and local differences in terms of the infrastructure and the economic development. What the village needs is an economic and cultural development, which will provide higher standard of living of the population.

Special attention has to be paid to the small enterprises in the rural communities and in the areas where unused capacities and human resources can be found. In the rural community it is very important to support the entrepreneur spirit of a larger number of rural households in order to achieve gradual transition from the traditional crafts and professions to involvement in the contemporary industrial activities. Investments for building infrastructure objects are needed, favorable loans for the people who will return to the village, tax relief and the like.

The village has a future only if the state, the local government and the rural population take care of the development of the rural community. The state and the local institutions can make a considerable impulse and contribution to the development of the rural community. The basic aim should be the joined performance in the support of the following processes:

- democratization and liberalization in the decisions of the authorities;

- decentralization of the rural development politics and implementation;
- promotion of the cooperation (cooperatives, associations, foundations) above the individualism;
- mobilization of the potential and development of the human capital;
- promotion of the economic, social and cultural quality of life for the rural population.

### *Investments in agriculture or in non-agriculture sector*

The investments are ones of the most important economic factors both for the overall development of the society and the economy and for certain areas and branches of the state economy. The following issues depend to a great extent on the range and dynamics of the agricultural investments:

- dynamics for implementation and extending of the contemporary agricultural techniques and technology;
- improvement of the quality of the human factor;
- the level of the exploiting of the natural resources (the soil, water resources by building of hydro-melioration systems etc);
- intensity of the process of concentration and centralization of the production;
- change and improvement of the agricultural structure (ownership and property) and the structure of the production for better crops, etc.

The slow intensity of the increase of the agricultural production is one of the basic structural problems of the Macedonian economy, because it has a negative impact on the: slowing down of the dynamics of the total social and economic development, deterioration of the balance of payments, constant increase of the agricultural products prices, slowing down the increase of the standard of the population, stagnation of the income from the agriculture compared to the other branches in the economy etc. From the many social and economic and technical-technology factors responsible for the condition of non-development of our agriculture, investments have had a great influence, since they are one of the most important factors for the development of every branch and area of the material production. Regarding this, a question could be asked, whether the insufficient investments in the field of agriculture were one of the basic reasons for the current structural problems in our society, that is to say a reason for the stagnation of the agriculture compared to the growing social needs.

The small range and the negative dynamics of the agricultural investments on a hectare arable soil, shows that the material conditions for intensification of the agricultural production were modest.

The bad position of the agriculture in the investments politics, i.e. the insufficient number of agricultural investments, results in slowing down the increase of the agricultural production, compared to needs of the social community which are rising, to satisfy the needs of the domestic market and to use the chance for export of our important agricultural products on the world market.

Starting from the social needs for faster agricultural development and the significance of the investments as a factor for development, the social community

has to provide favorable conditions for the agricultural development in the following period. Despite the improvement of the managing conditions, especially of the position of the agriculture in the primary distribution, for the sake of its own accumulation, supplemental sources of financing the broad reproduction of our (Macedonian) agriculture should be provided.

The management of the agriculture should be done according to the demand, not according to the factors of pressure, because by disturbing the balance between the demand and supply in favor of the demand a need for raising the quality level of the production is created.

In that way the agricultural policy should be oriented towards the customer, who is the only right indicator of the needs of the society, and each producer should aim to enter the essence of the modern management of today.

## **Trade policies, regarding**

### *Export or trade on the domestic market*

The level and structure of the agricultural export and import in Macedonia are determined by a number of factors: the natural conditions for the development of the agricultural production, climate factors, the structure of the agricultural production, the policy for economic development, the technical progress and the agricultural protection of the developed countries.

From the aspect of the structural changes in the interior trade in Macedonia, it is important to force high quality production of selected products and to enter the world market with these same products.

However, it is important for Macedonia to carry on with the intensive economic cooperation in the field of food production with the developing countries.

The development and improvement of the balance of payments in the agriculture with the foreign partners should be carried out by market policy and policy of prices. It should include the state reserves, the issues concerning the competition and the promotional approach.

The policy of prices, in accordance with the market rules of the international relations, especially the ones of the EU and WTO, should provide considerably smaller fluctuation of the domestic prices in terms of the prices in the international trade. The protection policy should be mainly based on guarantee and indication prices. As for the basic agricultural products, single prices will have to be introduced, according to which the state will purchase quantities equal to the required state reserves. The essence of this should be incorporated in the buyout, which will provide permanent income for the producers and permanent prices for the customers.

### *Import or import substitution*

The import of the agricultural-food products can be: a) free b) contingent (according to the quantity and according to the value) and c) seasonally limited.

The free import refers to the products that are not produced in the country or are produced in an insufficient quantity (permanently in short supply).

The import of the finished products that are in temporary short supply (wheat, oil, sugar, milk and dairy products, meat and meat products) should be under customs protection. The basic logic of the protective customs system is to equal the foreign prices with the domestic ones. The burden of the difference in prices falls on the back of the customer, but the producer is protected. For the possible import of agricultural products in Macedonia, only if agricultural products are exported from Macedonia, the policy should generally be pointed towards restriction of the imported shipments or partial reduction of the own import protection.

#### *Trade on the spot market or long-term shipment arrangements*

The trade on the spot is connected to the current survey of the market, because the producer must regularly and continuously follow the market, so as to know what is needed on a particular place, location, region or country. On the other hand, the long-term shipment arrangements in a way oblige the producer to become connected to a certain number of customers or user of his products and services for a longer period of time. So, both of the parties acquire mutual trust for providing the products (for the customer or the user of the products), or realization of the goods according to the agreed standards.

### **Farming, regarding some of the following questions**

#### *Investing in small-scale farms or in big agricultural properties*

In the developed capitalistic countries the process of concentration and centralization of the capital in all areas of the economy started long time ago, as well as in the agriculture. The large-scale agricultural farms easily deal with the competition compared to the small-scale ones. Yet in a period of crisis, the small agricultural producers (farmers) adjust faster to the new conditions. It is our opinion that the state should pass a law on minimum land, and that is land area in the economy under which the property must not be divided. The passing of such Law is necessary to stop the further poverty process of the rural population in Macedonia.

#### *Investing in the agricultural properties for unlimited or limited (seasonal) time periods*

As a result of the lack of legislative in the field of property law relations that will promote those agricultural producers who are pure farmers, we think that the state should support the real farmers (those who work full-time on the property in the agriculture). Although in some developed countries (Japan for example), the participation of the mixed agricultural economy in the total agricultural production is considerably high (over 40-50%). The pure agricultural economy has no other source of existence, so they have to use their labor, knowledge and skills to

organize the production, in order to survive and if possible to provide larger production for the market and for export.

#### *Investing in owner-operated or tenancy-based agricultural properties*

The question whether to divide the property to all of the children, or to keep it so that the oldest son will inherit everything, etc. has always been popular. For example, we will mention the institution called fidei commissum. It was introduced in England and Germany by the end of the 19<sup>th</sup> century. And thanks to it, the agricultural estates are transformed from free property of individuals into tied property of the family, which will be given to only one member of the family (usually to the oldest son who makes an oath), but he must not sell it or reduce it. The privilege of the fidei commissum is transferred from the father to the oldest son (primogeniture, majorate) or to the oldest male member of the family (seniorate) or to the youngest son (juniorate!).

The division of the economies in two or more heirs is unfavorable not only in term of making the property smaller, i.e. in terms of general weakening of the economic power of the property, but also in terms of the disability of the properties to consolidate and to organize production independently.

As far as the management of the property and the production is concerned, managers can run the production process, regardless of the fact that they will not be the owners of that farm.

#### *Investing in increased production or marketing activities*

First of all a marketing model of the approach and a concept for development of the production should be developed, and even after that one should start the increase of the production. The marketing concept is the basis of every modern organized production.

#### *Investing in trading skills or in farmer education*

The condition of the educational level of the farmers in Macedonia is such that they are not educated enough in the field that is their basic existence. A great deal of the farmers does not even have basic education. In some parts the age structure is such that it is very hard to organize modern educational process, except for some short-term training courses of any kind.

#### *Investing labor-intensive production or advanced technology farming*

The future lies in the modern technology. Investing in innovations will certainly pay off. In that way the low value primary products, which serve as a raw-material base for many different industries (textile, tobacco, leather, food and lately, fodder industry), will turn into high-value final products. The benefit of that type of investments is multiple: the value (price) of the product increases, there is possibility for new employment, the usage of the product is prolonged, etc.

Because of the tradition and the climate, in Macedonia there are crops that are labor-intensive (almost all vegetables) then, the production of fruit, grapes, as well

as all industrial crops (sunflower, turnip, tobacco) which serve as a basic raw-material for oil, cigarettes and etc.

### *Investing in advanced production technology or in farmer education*

The investments in this type of a model should be parallel, because the using of high technologies is proportional with the increasing of the educational level of the farmers. We can still give priority to the investments in high technologies, because the farmers will anyway rather learn the basic production techniques than learn to process their production. According to the principle of the market production, their products will be bought up by the processors, who will have to invest in modernization of the technical approach in the processing of the raw materials because of the competition.

### *Investing in animals, vegetables, fruits or cereals, etc. production*

Although the stock breeding production is based on a well-provided fodder, which means well developed grain growing, yet the most developed countries in the world, with highly developed agriculture, have a big proportion of stock breeding in the agriculture. For example, in Macedonia the participation of the stock breeding in the total agriculture is about 32%, which is a very low level. This percentage in Denmark, Ireland, The Netherlands and other countries is double and it is above 60%.

### *Diversity or specialization of the agricultural production*

Because of the insecurity of the placement of their products, the agricultural farmers are forced to be oriented towards diversity. In that way they start to grow everything, which does not give them many advantages. This is their reasoning: if I fail with one product that will be compensated by another product. But, science shows that specialization in the agriculture is inevitable. And this means that the producer must choose one basic (main) product and possibly some subsidiary products (for example if he owns his property, to provide fodder for the cattle on his own).

### *Borrow and invest or save and invest*

The best way of investing is by saving. Republic of Macedonia has more than 600 million Euros of personal (internal) savings, but because of the lost trust in the state institutions, the people withdrew their money from the banks. This money is the basis, which the country must put into function if it wants to get over the monetary crisis. By reducing the tax or by temporary exempt of part of the taxpayer, at least those from the passive hill and mountain regions, this money can be invested for modernization of the production.

### *Processing and marketing by organizations owned by the farmers or by private firms*

The farmers cannot produce and process their products. That is why it is best to establish a system of integration. This means that according to the principle of interest of the market, the producers should buy out from the farmers and should process the products from the primary sector. In that way they will direct the

farmers to what the market needs. And as far as the form is concerned, it would be best if it could be an organization of farmers that will protect their interests, before the Government or the processors. Private firms could run the marketing, but it would be more efficient if it could be organized by their own organization. The interest would be greater, because of the mutual risk.

## **Conclusions**

The agricultural policy in R. Macedonia, from its independence till today, has been conducted in restrictive macro-economic conditions and in a state of its transformation and adaptation to the rules of the WTO and CAP reforms of the EU.

The adaptation of the agricultural policy in the trade policy and the price policy according to the rules of the EU and WTO should be reflected in the increasing of the budget. However, the agreement for associative membership, based on the clause of most privileged nation and on the asymmetrical trade, should reduce or totally eliminate the differences of the import prices of the input and export prices of the output, by resources of the Fund for guarantee and directives of the EU, and by the prescribed possibility for autonomy of the developing countries in their determination of the level of reducing the customs of certain products and support of the production. Abandoning the prescribed possibilities, results in extremely fast liberalization, which will certainly cause disastrous consequences on the agricultural development.

## **Recommendations**

The positive direction of the competition should move according to appropriate structural changes (bigger farms), high modern farmer education, better technique and organization etc.

The promotional approach should exploit all available elements of transparency of the products, of readiness for merciless competition (in terms of quality and price) on the world market.

One of the most important prerequisites for the development of our economy is the attraction of direct foreign investments. The deposit of foreign capital will depend on the conduction and completion of the trade reforms. Because of the territorial size of our market, Macedonia cannot attract market-oriented investments. The only optimal platform is the export.

The multipliable positive effect of the direct foreign investments will contribute to the development of a net of side activities and services, reduction of the unemployment (which is 30%), improvement of the banking sector, and also increasing the international credibility of the country on the whole.



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**Impact and Consequences of a Future EU  
Accession for the Macedonian Agricultural  
Sector**

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## **Abstract**

The study clarifies the present Macedonian agricultural policy and analyses the consequences of future policy options for Macedonia, outside as well as inside the European Union. The present Macedonian agricultural policy is socially costly, favoring farmers at the expense of consumers and taxpayers. The highest cost is related to the import protection policies. Macedonia fails from taking full advantage of its comparative advantages, consisting of huge amounts of cheap labor and cheap land. From a food sector point of view, Macedonia loses from joining the EU compared to a free trade scenario. The main reason is that the Common Agricultural Policy – the CAP - of the EU will raise food prices above world market levels. On the other hand, Macedonia gains from joining the EU compared to continuing with the present high price policy on food in Macedonia.



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## The Problem

Macedonia may in the future enter the EU. Such a membership will have far-reaching consequences for the Macedonian economy in general and the Macedonian agriculture in particular. This paper focuses on possible effects of the EU membership on the Macedonian agriculture, compared to a non-membership case.

## The Methodology

We start by presenting a theoretical basis for the analysis. After that we examine experiences from previous EU accessions, continuing by highlighting fundamentals of the CAP as a basis for speculations about the future of that policy. Finally, we try to estimate the possible welfare consequences of different options of a future Macedonian agricultural policy. We end up in some conclusions regarding agricultural policy strategies related to trade and to farming.

## The Theoretical Background

Our theoretical framework basically is the traditional neo-classical economic approach, found in standard textbooks in economics. When discussing the functioning of a market, a fundamental underlying assumption is that there exists some kind of *legal structure* that is able to protect individuals and property rights. In modern societies this structure normally is provided by the state. Market transactions should be understood as *voluntary actions of free individuals* - forced actions and actions under threats are not included in the market concept.

The ultimate purpose of a *market* is to co-ordinate consumers' willingness to pay with suppliers' willingness to sell. That is a huge task, taking into account the vast number of daily transactions taking place between a vast number of unique consumers and numerous unique producers/suppliers. The dominant market transaction is a *bilateral ex-change of property rights*.

The most decisive purpose of the *world market* is to work as a reference point, determining the opportunity costs of agricultural policies. Even if world market prices on agricultural commodities often are to be considered as dumped prices, they nevertheless represent the prices nations have to accept in importing or exporting their commodities. That is why world market prices generally are used as *reference prices* in economists' welfare calculations.

To succeed in co-ordinating markets, individual decisions (to consume or to produce) must be based on market *prices*. The basic meaning of prices is thus to clear markets, thereby offering crucial information in a very condensed form. If prices go up, consumers generally reduce consumption while producers raise their

production/supply, and vice versa. In a closed economy, a surplus (excess supply) normally results in reduced prices and a deficit (excess demand) in raised prices. No governmental agency is able to foresee those prices that establish market equilibriums. The explanation is that information about those costs and the willingness to pay, that market actions are based upon, are known only by the individual market actors themselves, i.e. representing a kind of information impossible to collect for a public agency. Even if a public agency had the ambition to collect such data, it would never succeed, since much of that information is unknown also to the individual consumer, up to the point when he/she actually buys a certain commodity, or to the unique producer until he/she eventually sells a product. In this way, the information is created exactly when the transaction takes place, and can't be revealed unless the actual choice really is made.

That conclusion is easily illustrated by the important concept of *opportunity cost*. Only the individual himself, let say a farmer, knows the opportunities he loses in being a farmer. The labour cost in producing wheat should be based upon the salary he could attain in the best alternative to being a wheat farmer. If that is being a professor, the opportunity cost is high. Would he otherwise be unemployed, the opportunity cost could be close to zero. In this respect, opportunities forgone are unique to each individual.

Welfare calculations made in this paper are based upon the willingness to pay and the opportunity costs, as they are represented in the demand and supply curves, as well as upon prevailing prices. *Social welfare* is the sum of consumer, producer and governmental surpluses. *Consumer surplus* is the area below the demand curve and above the price, while the *producer surplus* (profit plus fixed costs) is the area above the supply curve and below the price. *Governmental surplus* generally is represented as the budget consequences.

*Agricultural policy* normally influences prices. To do so is a costly thing to society, unless the policy corrects so called market failures, which seldom seems to be the case. The basic cost of price distorting policies, is that it disturbs the market co-ordination and information-providing role of price, as mentioned above. As a consequence of this, agricultural policies can't be explained in terms of rational behavior in order to improve social welfare. It seems best understood, and explained, in terms of *power* exercised by politically powerful *interest groups* in society. In developed countries, farmers are considered powerful on the political arena, able of transferring wealth from other groups of society, usually consumers, taxpayers, unemployed and poor people, to themselves. The ultimate gainers of such policies are the *landowners* and, within the EU, also the "*quota-owners*".

The basis for national specialization of production in economic theory usually is the concept of *comparative advantages*. One way of defining those is to say that a country has a comparative advantage in a commodity if it (without policies) can export the commodity at prevailing world market prices. If the country without any policies imports the commodity it has a *comparative disadvantage*. To gain from international trade a country should export commodities in which the country has comparative advantages.

## Experiences from Previous Accessions to the EU

Referring to Rabinowicz & Bolin (1998), experiences from four previous expansions of the EU tell us that no agricultural sector, in no accession process, seems to have lost its pre-accession political support, so far. That implies, however, that individual countries, like Finland, may have to pay a large share of the agricultural support themselves. That also means that the CAP, generally claimed to be a *common* policy, gradually over time has become *partially renationalized*, taking into account diverging national characteristics. As countries may differ very much according to agricultural conditions, new members means new rules, implying that new countries tend to put their own footprints to the CAP. That also means that the CAP is flexible and the EU is innovative in incorporating new means of agricultural support.

Common prices from first day of accession are nowadays given the highest priority, meaning that no transitional arrangements according to price levels will be permitted. Other means of support are proposed to become increasingly decoupled from existing levels of production. Production quotas and arable land levels, eligible to direct payments, have been determined according to pre-accession levels, 2-3 years before the point of accession, implying that most new member countries don't have to adjust their prevailing production levels. It seems, furthermore, not possible to deteriorate conditions for agriculture in incumbent member countries, reflecting the importance of not changing existing agricultural policy rules – as represented in the *acquis communautaire* - in membership negotiations.

For the Eastward expansion of the EU, its fifth expansion, it seems unlikely that a mechanical application of existing CAP-rules will be applied. As the expansion is costly for incumbent members, some cost-reducing efforts will probably be searched for. One of these is the gradual introduction of direct payments to accession countries. Another one is reflected in the Mid Term Review – MTR - proposal, implying decoupling, modulation and a gradual reduction of the direct payments over time. Nevertheless, the outcome of accession negotiations must become a mutually beneficial solution to all the countries concerned, since the newcomers enter by free will and must be accepted by the existing members.

## Basic Elements of the CAP

The CAP is a producer-oriented policy, supporting farmers at the cost of food consumers and taxpayers. Welfare economic analyses generally show that the policy is costly for the EU as a whole, as consumers and taxpayers lose more than farmer's gain. Individual countries, generally the "natural" food exporting ones, may, however, achieve a social gain from the policy, especially when they receive more from the EU budget than they pay to it. Losing groups are also the non-member countries, especially food exporting countries that have to climb the tariff walls around the EU, as well as receiving lower world market prices than

otherwise. Also, environmental interest groups may suffer from pollution caused by the policy-induced, high intensity farming methods in the EU.

The CAP basically consists of *price support* means (like boarder protection measures and intervention prices), *direct payments* (to land and animals, as well as to environmental and rural development), *supply management* measures (like quotas and "subsidy rights") and a wide set of *rules* for farmers to become eligible of the political support (like set aside and cross-compliance rules). The outcome of this, as measured by the Producer Subsidy Equivalent - PSE - concept, is that 35-50 per cent of farmer's gross revenues consist of political support, in one form or the other.

The policy follows three basic principles. One is the *community preference*, resulting in common boarder protection rules against non-member countries. The second principle is the *common market*, securing free trade conditions amongst member countries. The third one is the principle of *common financing*. These principles, however, can't be derived from the officially objectives of the policy. In these objectives are stressed the importance of a fair living standard of farmers, food security, stable and reasonable food prices, as well as raised productivity in farming. Actually, none of the used principles, or measures, of the CAP is efficient in attaining those objectives. The final outcome may very well turn out to be the opposite, implying that the policy may have reduced the welfare of farmers, may have reduced the food security, may have raised food prices and, for sure, has reduced the international competitiveness of EU farmers.

## Future of the CAP

Looking at the 40-year long history of the CAP, it seems obvious that the Mac Sharry reform of 1992 implied a turning point in its development. While the early policy heavily relied upon price support, the Mac Sharry reform introduced a reduction of price support measures compensated by direct payments. The Agenda 2000 reform of 1999 can be characterized as a repeated Mac Sharry reform in that sense. A new turning point seems to be introduced with the on-going MTR proposal, in trying to decouple agricultural support from production. In this case, farmers are proposed to get a direct support *per farm*, calculated according to what they produced on that farm in the period 2000-2002, implying that future support will not be related to what actually is produced. To improve the competitiveness of EU agriculture, future production should be governed by the world market prices only.

Related to the decoupling, however, measures of "cross-compliance" are proposed, implying that farmers must stick to environmentally friendly production methods, to food safety rules and promoting rural development, to become eligible to the direct support. That is a way of "re-coupling" farming support, not to prices but to certain rules of behavior. The MTR also proposes modulation, meaning a gradual transferring of money from large farmers to smaller ones, as well as from

market price support (first pillar of the CAP) to environmental and rural support (the second pillar).

It seems obvious that the MTR policy proposal will create difficulties with the external and internal legitimacy of the CAP. *Externally*, farmer support will be linked to historical production – a kind of compensatory approach. The question is for how long a period ordinary citizens of society will accept that kind of budget transfers. Can farmers be paid for what they did 10 years ago, 20 years ago or 100 years ago, without taxpayers wondering what they are paying for? The policy is especially demanding in a situation where budget means are scarce and other groups of society – e.g. unemployed, old and sick persons - increasingly will ask for public support. These groups will, furthermore, over time pay less to the public budget.

It seems impossible to reasonably co-ordinate the present support structure with a future structure reflecting true environmental and rural development needs. It is not probable that those farmers and regions that actually got the support in 2000/2002 are those farmers and regions that in the future should be paid for their environmental and rural contributions. That means that the present support structure – over farmers and regions - should be radically re-structured to make the cross-compliance efforts justifiable to the public audience, i.e. the taxpayers.

The *internal* legitimacy of the policy will be reduced in the sense that farmer groups internally will compete for the support. As long as agricultural support mainly was a *price* support, it was a common interest of *all* farmers to raise the support. When scarce budget means must be distributed amongst farmer groups, as proposed in the MTR, the competition between farmers will reduce their ability to talk with “one tongue” against politicians - what one farmer will get another farmer will lose.

Consequently, with the MTR proposal the future of the CAP really is at stake. Even if the MTR in its present form will become altered in the policy making process, its major principle of decoupling may very well come true, implying a decisive change of the policy. A future Macedonian accession therefore means a radically different agricultural policy from the present CAP. The major differences concern the degree of decoupling, as well as the size of direct payments. However, a “true” decoupling of support from production may be hard to achieve, some kind of *partial* decoupling is more probable.

## **Point of departure**

### **Some basic facts about the Macedonian agriculture**

178 000 *private farmers* produce 70-80 per cent of Macedonian primary production, using 460 000 hectares of arable land, which constitutes 73 per cent of total arable land area, implying an average size of private holdings of 2.6 hectares. As private farmers only use 229 000 of their hectares, the average size in reality is even smaller, i.e. 1.3 hectares per farm, leaving 50 per cent of the land unused.

About 50 per cent of private farmer production is marketed - the residual is consumed within farmer households.

The number of *agricultural enterprises* (agrocombinats) is around 200 units. Their number is decreasing according to the privatization process, in which some of them are closed down. Statistics concerning these enterprises are unclear (Galev and Dimitrievski, p. 61 and Galev and Murarcaliev p. 57, 2001). According to some figures these combinats use slightly more than 600 000 hectares, of which more than 75 per cent is pasture (Galev and Dimitrievski, p. 62 and Galev and Murarcaliev p. 62, Table 26, 2001). Depending on the statistical source and the basis for calculation, the agrocombinats might have an average size between 3 000 and 1 000 hectares of arable land. If the higher figure is correct, the agrocombinats seem less efficient than private farmers. If the lower figure is correct, the two farming sectors may be equally efficient.

There also exist around 80 agricultural cooperatives, cultivating slightly less than 4 000 hectares (Galev and Murarcaliev, p. 59, 2001). We may also note that the total cultivated area in Macedonia steadily has been declining, at least since the 1960s - now at an annual rate of more than 3 per cent (Galev and Murarcaliev p. 63, 2001).

As labor unemployment is high in Macedonia, especially in rural areas, the cost of the labor-intensive private farm production is low from a social point of view, while the capital-intensive production of enterprises seems comparatively costly. That tends to increase the comparative advantages of private farmer production over enterprise production.

Macedonian agriculture today benefits from a rich supply of cheap land and cheap labor. Production within the private farm sector is labor intensive and seems comparatively efficient. The capital-intensive enterprise production may be less efficient from a social point of view, suffering from internal organizational problems, low productivity and high production costs. As Macedonia is a net importer of agricultural commodities, it presently does not seem to have comparative advantages in agricultural commodities. The net export revenues must in that case be captured in other branches of the economy.

### **What Do We Know About Macedonian Agricultural Policy**

The Macedonian agricultural policy is divided among three different Ministries. The Ministry of Agriculture, Forestry and Water Economy is responsible for policies concerning primary production and rural development, while the Ministry of Economy not only controls policies for the food processing industry as well as credit and investment policies for the agricultural sector, but also finances intervention measures through the Bureau of Market Reserves. Foreign trade policies are administrated by the Ministry of Foreign Affairs (Galev & Murarcaliev, 2001). This division causes conflicts between policies, especially when, as in the previous coalition, the government consisted of ministers from different parties (Azderski, 2002).

### *General objectives*

In 2001 the Ministry of Agriculture, Forestry, and Water Economy accepted “The Agricultural Development Strategy in the Republic of Macedonia to 2005” (Galev & Murarcaliev, 2001, below referred to as the Strategy) as the policy strategy for the coming years (Georgiev, 2002). Suggestions put forward here are, however, more to be regarded as “visions” than explicit policies. The Strategy contains much on objectives and problems that need to be addressed, but only sweepingly mentions solutions or measures to be used.

The government’s aim to become a member of the European Union is evident, both in the signing of the Stabilization and Association Agreement and in the Strategy.

Among the general aims are mentioned: a positive growth rate of the agricultural sector’s share of GDP, an increased domestic and foreign demand for Macedonian products and (through import tariffs) encouraging traders in the marketing of domestic produce more efficiently, instead of turning to imports.

The intermediate aims (up to 2005) are claimed to be: to better use and preserve human and natural resources with a “medium” intensive use and growing competitiveness, to better meet domestic demand for low-priced, high-quality food and to export fresh and processed agricultural products.

### *Specific objectives*

The Strategy comprises five policy areas: production, market and price, structural and rural concerns, agro-environmental questions, as well as agricultural education.

#### Production Policy

The main objective of the production policy is to achieve a high degree of Macedonian self-sufficiency, assure surpluses for export and to transform land into private property.

#### Market Policy and Price Policy

The stated objectives can possibly be interpreted as:

- free trade with the EU and the WTO countries,
- exports of competitive products with export subsidies,
- imports of EU-subsidized products in short supply, e.g. raw materials and equipment,
- to adapt production to the standards of the EU and to the rest of the world,
- to ensure that production meet domestic and foreign consumer demand.

Free trade with the EU and WTO countries is not considered possible until self-sufficiency is achieved and when the Macedonian agricultural sector productivity is in line with average world productivity.

The market policy also aims at achieving foreign trade balance, without creating unfair competition against domestic producers, through seven policy measures (Galev & Murarcaliev, 2001, p.149):

- “turn non-customs barriers into tariffs;
- decrease subsidies and import barriers through gradual elimination of domestic support for farmers;
- define the necessary import of equipment and raw materials;
- protect the agriculture from unnecessary imports which would unjustifiably burden the foreign trade balance;
- implement world quality standards;
- have an intensive export of quality and healthy goods
- use the price system, the instruments and the measures of the market policy.”

#### Rural Policy

There are also rural policy aims, e.g. to keep all villages populated, especially in the remote mountainous regions, to increase the use of arable land by small farmers through support and to restore existing, as well as building new, systems for irrigation and drainage.

The rural policy should be expanded by increasing ecological and recreational activities through (Galev & Murarcaliev, 2001, p.149-150):

- “introduction of organic farming;
- maintaining semi-natural habitats;
- raising Alpine cows;
- promotion of farm systems with low investments in less favoured areas of high natural value
- introduction of integrated environmental aspects in the common European market by giving direct payments conditioned with environmental provision and;
- coordination of programmes, etc.”

#### Educational Policy

Policies should provide the same security and benefits to farmers as to other rural businesses, as well as strengthening the education in new technology, marketing, management and product development (including quality aspects, packaging and design).

Agricultural enterprises should be supported in their transition process, since they are considered central for the development of the agricultural sector as a whole. Moreover, it is claimed that the definition of cooperatives should be changed with a new law to increase their status. Small farmers should be supported through an Agribusiness Centre that provides education, advising and accounting monitoring.

The Strategy suggests introducing short-term investment loans and a partial cancelling of debts. A land programme to counteract the land fragmentation is also considered necessary.

### *Measures*

Some of the “objectives” in the previous section are actually to be considered as measures. The measures used by the Ministry of Agriculture, Forestry and Water Economy, during the second part of the 1990’s, has shifted from direct price subsidies to the Programme for stimulation of agricultural development. The latter receives some 75 per cent, or EUR 7.4 million, of the budget in 2001. Nearly half of these money goes to health protection of plants and animals, while most of the remaining EUR 3.9 million is allocated to the Extension Service. In addition, the Ministry distributes funds to programmes for revitalisation of the countryside. Even though the investment-programme received about 60 per cent more money in 2001, it is considered to be only “symbolic” by researchers in the agricultural sector.

Even if no budget entry refers to direct price subsidies, at least wheat receives a subsidy of 2.5 MKD/kg, paid to small farmers, as well as an additional subsidy for transportation costs of 0.50 MKD/kg, a subsidy given to all wheat producers. In the budget proposal for 2003, the Ministry of Agriculture, Forestry and Water Economy suggests price subsidies for six specified products, including wheat, tobacco, cow and sheep milk (Ministry of Agriculture, Forestry, and Water Economy, 2002). Researchers estimate that 5 to 20 per cent of production costs are subsidised (Azderski & Gjorgjevski, 2002; Georgiev, 2002).

The Ministry of Economy has at least two agencies involved in administrating the budget for agricultural policy. The Bureau of Market Reserves intervenes to create stability in the market for wheat and tobacco, as well as for some other products. At a guaranteed price - for wheat 10 MKD/kg - the bureau buys up the surplus and stores it until a shortage arises. For fresh products, like vegetables and fruits, the surplus is used for public consumption, for example in hospitals and schools. The budgeted funds exhibited a decreasing trend in the second part of the 1990’s. However, in 2001 it was increased four and half time, becoming more than EUR 8 million.

The Bureau for Economically Underdeveloped Regions administrates a Republic Fund as a means to stimulate multi-sector rural development. The agricultural sector receives a “significant portion” of its money. The allocated money has increased in recent years, and in 2001 the Bureau obtained EUR 9.5 million for all economic sectors of Macedonia.

### *International Relations*

The foreign trade policy has changed significantly during the last decade. Export subsidies were abolished in 1996, following recommendations from the World Bank (Angelova, 2002). Nevertheless, transport costs for exports are subsidised, e.g. for tobacco and tobacco products.

Macedonia has trade agreements with most European countries, e.g. the earlier mentioned Stabilisation and Association Agreement, SAA, with the EU, which allows for trade liberalisation of agricultural products. Still, some limitations like import quotas and tariffs will apply to certain products during a 10-year period.

Table 1 shows agreed quotas and tariff rates in accordance with the SAA. Present agricultural support implies a Macedonian PSE-coefficient of at least 67 per cent - the PSE of EU being 35-50 per cent.

Table 1. *Import taxes for some products from the Official Gazette and the Stabilisation and Association Agreement with the EU (Source: Galev & Murarcaliev, Table 69, p.133, 2001.)*

Products	2001		2002		2003	
	Quota	Rate	Quota	Rate	Quota	Rate
Wheat		20 %				
Flour		25 %				
Maize <sup>a</sup>	20 000	90 %	20 000	80 %	20 000	70 %
Rice		60 %				
Crude oil <sup>a</sup>	5 000	90 %	10 000	80 %	15 000	70 %
Non-refined and Regular sugar <sup>a</sup>	5 000	90 %	10 000	80 %	15 000	70 %
Tomatoes and peppers		40 %				
Apples		60 %				
Table grapes		60 %				
Beef		18 %				
Lamb	No restrictions					
Pork <sup>a</sup>	2 000	90 %	2 000	80 %	2 000	70 %
Poultry meat <sup>a</sup>	1 500	90 %	2 000	80 %	3 000	70 %
Cow's milk		25 %				
Powder milk <sup>a</sup>	200	90 %	300	80 %	400	70 %
Cheese and cheese-cream <sup>b</sup>		80 %		65 %		50 %
Eggs		40 %				
Wine <sup>c</sup>		50 %				
Oriental tobacco <sup>d</sup>		30 %				

<sup>a</sup> The customs rate is applied when the import quota is filled. Determined by the Stabilization and Association Agreement.

<sup>b</sup> % from most favoured nation clause.

<sup>c</sup> Special agreement within the SAA.

<sup>d</sup> Without customs (import)

Macedonia also has free trade agreements with other Balkan countries and the EFTA. The closest co-operation is with Croatia, Bosnia-Herzegovina, Yugoslavia and Albania in a special alliance, named the Stabilization and Association process (Hegarty, 2002).

Macedonia became a member of WTO in October 2002 and will have 3 years to comply with the WTO rules. The country has been permitted to support an agricultural product up to 5 per cent of the value of production. Macedonia may also subsidize non-productive inputs with up to 5 per cent of the value of total agricultural production.

## **Major Problems and Expansion Routes in the Macedonian Agriculture**

Macedonia is a land and labor abundant country suffering from high unemployment rates, high prices on capital, scarcity of modern capital technology and a modest growth rate in the economy. Partly, that has to do with the transition from a socialist to market oriented economy, partly is has to do with the institutional structure, the prevalent price structure and the existing policies.

In the agricultural sector our hypothesis is that Macedonia should take advantage of its cheap land and labor, concentrating on commodities using those inputs, e.g. commodities like fruits, vegetables, sheep, wine, etc. Furthermore, agricultural policies should be radically changed, as the sector should be run at world market prices, which are lower than the existing ones. That will probably reduce production levels of almost all commodities, reflecting the present comparative disadvantages of the Macedonian agriculture. Macedonian comparative advantages are, at least to start with, most probably to be found in low priced, low quality commodities with a large content of labor and land inputs, consumed domestically and in some cases exported to neighboring countries.

That means that Macedonia has to start with “a low port of entry policy”, as it just now can’t afford to enter and invest in the exporting of high quality commodities to distant markets. In a long run perspective Macedonia might enter the higher priced markets, e.g. through a gradual development of networks and investments in trading technologies. What Macedonia needs more of now seems to be: time, learning by doing, modern laws according to property rights, macro economic stability, raised capital funds through internal savings and relevant price incentives. Instead of agricultural policies, Macedonia needs policies for rural development, food policies (hygiene, processing, re-structuring), environmental policies, as well as a general support system to business development and education.

Entering the EU might help in some respects and be a problem in others. The point of entry may, however, be in a distant future, implying that Macedonia must do something on its own during the pre-accession period.

What is most urgently required for economic growth in general is the creation of free and functioning markets, especially the market for farmland. In order to enhance structural change and economic development in farming it must be possible to freely sell and buy land, i.e. market actors must be completely convinced that the future income stream from farming that land, strictly belongs to the owner. A securing of such a property right must be given the highest priority amongst policy makers, since it is hard to foresee a positive development in agriculture without well defined and legally stable property rights to land.

## Welfare Consequences of Seven Policy Scenarios

This section is based on the Ericson (2003) study. The basic approach in studying the welfare consequences of future policy options for Macedonia can be illustrated as in figure below. The reference point is free trade, implying that prices inside Macedonia are represented by world market prices - the  $P_W$ -line. If, for instance, Macedonia itself, outside the EU, sets its internal price at the EU level - equal to the  $P_D$ -line - farmer gains are represented by the area  $a$ , while consumer losses are represented by areas  $a+b+c+d$ . As the government can collect import tariff revenues equal to area  $c$ , there is a net social loss equal to areas  $b+d$ .

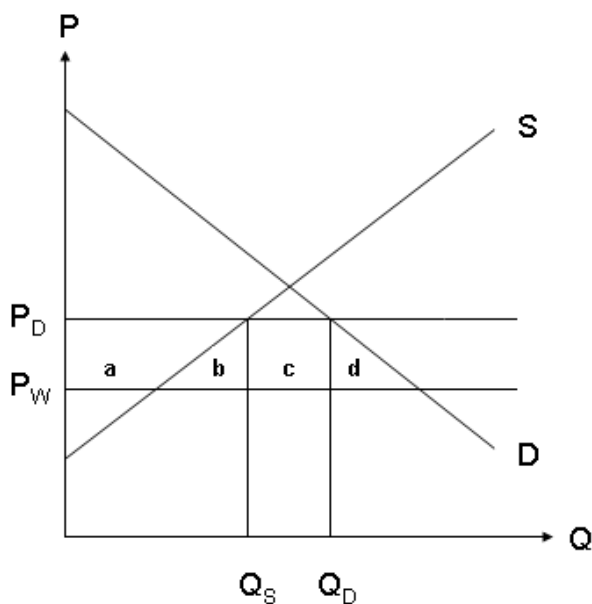


Figure 1. Welfare consequences of different policies

On the other hand, if Macedonia joins the EU, welfare consequences for farmers and consumers are as above. There are, however, no governmental gains from tariffs, meaning that the net social loss consists of areas  $b+c+d$ , representing a greater loss compared to Macedonia staying outside the EU, since Macedonia in that case can not collect any tariff revenues.

All the presented policy scenarios will be compared to a reference scenario equal to the Free Trade scenario (i.e. the  $P_W$  prices) and calculated as the summarized change in welfare outcome for two periods of time. One is the period up to the EU membership entrance, assumed to be 2003-2016, and the other one is the period after 2016. For the pre-accession period, Macedonia can choose four options: Free trade, Agenda 2000, New Reform or National Policy. In the second

period one option is to continue with free trade in all cases, but for the Agenda 2000 option there also is the possibility to continue with Agenda 2000. Also the New Reform can be continued after 2016, while the National Policy can be continued with Agenda 2000, the New Reform, as well as with Free Trade.

As we use the Free Trade option as a reference point for all scenarios, all figures are shown as differences from the Free Trade option, implying that the number of scenarios is reduced to seven policy paths over time, see Figure 2 below.

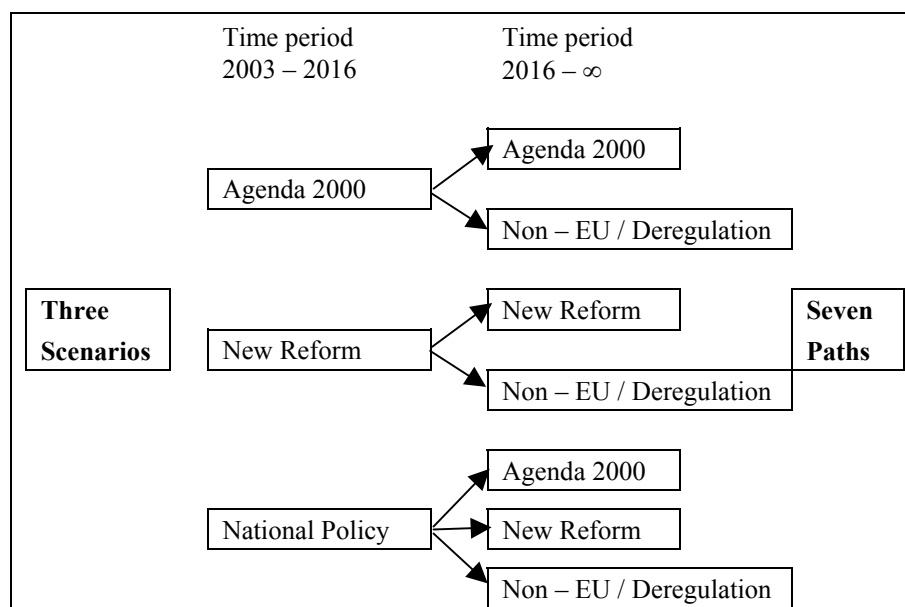


Figure 2. Seven scenario paths. In the first period, 2003-2016, Macedonia chooses between three different scenarios (seen as deviations from free trade). In the second time period, 2016-∞, there are two options for the first two paths, continuation of respective CAP-scenario or Free Trade; while the third has three possible alternatives: Agenda 2000, New Reform or Free Trade.

Using prices, elasticities, discount rates and consumption and production levels as shown in Ericson (2003), the welfare outcome of the different policy options are as in Table 2.

Table 2. Summary of the discounted outcomes for the different scenario paths (Source: Ericson, 2003.)

Deregulation		+/- 0 EUR
Agenda 2000	Agenda 2000	- 868 MEUR
	Non – EU/Deregulation	- 183.5 MEUR
New Reform	New Reform	- 440 MEUR
	Non – EU/Deregulation	- 46 MEUR
National Policy	Agenda 2000	- 1 100 MEUR
	New Reform	- 786 MEUR
	Non – EU/Deregulation	- 392 MEUR

## Analyzing and Discussing Scenario Outcome

As all figures in *Table 2* are negative, it seems obvious that the best policy for Macedonia is the free trade policy. The explanation is that Macedonia is a net importing country in food commodities, implying that consumers lose more than producers gain in deviating from free trade. The most expensive scenario is to run the existing policy (the National Policy) up to the membership point in 2016 and then join the existing version of the CAP, i.e. the Agenda 2000. The explanation is that such a strategy would hurt the consumers the most through its high food prices.

The smallest loss to society, when compared to the Free Trade scenario, is caused by the New Reform scenario, followed by the Agenda 2000, and finally the National Policy scenario. The classification makes the Agenda 2000 scenario path less interesting since it only constitutes an intermediate position between the others. The Mid Term Review proposal by the EU Commission resembles the New Reform scenario, and even though it is not certain that it will be fully implemented, it also reduces the importance of the Agenda 2000 scenario as a prediction of the future CAP. The remaining motive for the Agenda 2000 scenario is Macedonia's attempt to mimic the present CAP in stated reform proposals.

It is pertinent to consider the results for the non-entry paths, particularly since the net loss to society from an introduction of a CAP policy that not is followed by a EU-membership, implies an unnecessary cost. If Macedonia implements an Agenda 2000 policy mix during the pre-accession period, that is not followed by an accession to the EU, the country will lose EUR 183.5 million, which is eighteen times as much as the budget for agricultural support for the Ministry of Agriculture, Forestry and Water Economy in 2001 (Galev & Murarcaliev, 2001). Even though producers will gain EUR 0.5 billion, consumers will have to pay more than EUR 1 billion extra for eight important food commodities, during the "waiting period" of 13 years. The higher share of the national household budget spent on food implies lower demand for output from other sectors of the Macedonian economy, causing farmers to expand at the expense of the manufacture and service sectors. Notwithstanding the positive change in government surplus, the raised import revenues cannot fully compensate consumer losses in such a scenario.

The analysis consequently shows that if Macedonia, for one reason or another, wants to join the EU, the best policy before the entrance is to introduce free trade in agriculture during the pre-accession period and, just at the point of entrance, introducing the actual CAP, whatever it looks like. Seen only from the food sector point of view, the best policy is to introduce free trade and to stay outside the EU. The gain of doing so may be as high as EUR 1.1 billion.

The ranking of the scenario paths remains unchanged if a discount rate of 20 per cent (reflecting a high uncertainty of future events) is used instead of the basic 5 per cent. The lower importance of costs and gains in the second time period, however, results in a smaller difference between the EU-accession alternative and the non-entry one. Consequently, if the loss or benefit to future generations is not

considered significant, the question whether to enter the EU or not, declines in importance.

The choice of elasticities influences the results. If, for example the price elasticity of demand is higher than the chosen -0.5, consumer losses would be even larger, while the government would gain more, resulting in a greater net loss to society. For a demand elasticity less than -0.5, the results will be the opposite.

Supply is unaffected by the change in price elasticity of demand. On the other hand, if the supply elasticity is more elastic than the chosen 1, producers will gain less. A more inelastic supply will give the opposite results. However, even if the values of the elasticities determine the welfare outcome, the ranking of the scenarios seems robust to changes in elasticities.

Some commodities dominant the outcome: wheat, milk and sheep meat, with beef meat not far behind. These goods bring about the largest changes in surpluses in all policy scenarios, especially for producers. That partly infers to their importance in agricultural policy, and partly to their large quantities in consumption and/or production.

There may be several reasons why two prices – those for maize and oilseed - in the National Policy scenario are lower than the world market prices. First, the EU reference price may be an inaccurate estimation of the world market price that Macedonia will meet in reality. Second, it can be a reflection of quality differences in commodities between the EU and Macedonian markets. Finally, Macedonian consumption of maize and oilseed commodities may be subsidized, e.g. a low price on maize could indicate that pig producers receive a cost-reducing input-subsidy.

The model has limits in its possibilities to make accurate estimates of the welfare outcome for the policy scenarios. A better access to first-hand statistical data, econometrically estimated demand and supply elasticities, as well as demand and supply functions, would improve the accuracy of the model. Nonetheless, results in the analysis seem to support the hypothesis that the Macedonian choice of its agricultural policy is significant to social welfare.

## **What is Best for Macedonia According to**

### **Basic strategies, regarding**

#### *Governing agriculture by demand driven factors or by push factors*

Agriculture should be driven by demand factors, i.e. by prices reflecting consumer willingness to pay and individual opportunity costs, since no central agency is able to collect the needed information to control all factors relevant to individual decision-making. No push factors derived from politics are desirable, unless they are correcting so called market failures.

#### *Accelerating or retarding movement of people from rural to urban areas*

There is no need for increasing the pressure from push factors in farming, e.g. through increased investments in modern technology, for the same reason as given above. The first best policy is to make use of unemployed rural people in the labor and land intensive part of the farming sector.

#### *Investing in non-agriculture or in agriculture*

Scarce investment funds should in the first place be used to improve the infrastructure, alleviating transports and trade. Also important is to improve the institutional structure and to raise education levels generally. All such investments will alleviate rational individual decision-making.

#### *A consumer or producer oriented agricultural policy*

Agricultural policy should consider the welfare of farmers as well as the welfare of consumers and taxpayers, accepting the fact that consumer and taxpayer interests generally outweigh farmer interests. The ultimate purpose of production is to fulfill consumer needs, especially in a food importing country, where farmers ability to contribute to social welfare through raised production may be limited.

### **Trade policies, regarding**

#### *Exporting or selling on the domestic market*

Macedonian farmers main task is to produce for the domestic market as cheap as possible. Some commodities qualify for exports, but that activity probably has to start with “a low port of entry”, i.e. selling primary commodities cheaply. Macedonian farmers should accordingly produce for those consumers that are willing to pay for the products and the quality that they profitably can produce.

#### *Import or import substitution*

From a social welfare point of view, imports are to be preferred to supporting domestic production through import protection. The reason is that we consider world market prices as reflecting the true social opportunity costs. Import tariffs unnecessarily increase consumer costs.

#### *Spot market sales or long-term delivery contracts*

As it generally takes a long time, and much of investments, to build up contract systems for durable and long-term deliveries on export markets, it may be necessary to gain time by selling at lower prices on spot markets.

#### *Exporting primary (low price) or upgraded (high price) commodities*

As Macedonia now seems to have limited possibilities to process and to guarantee large and constant volumes of upgraded commodities with high quality, a fast and beneficial start seems to be to start by exporting not very upgraded primary products.

## **Farming, regarding some of the following questions**

### *Investing in small or in large farms*

Family farms generally seem to be the most efficient organizational form in primary production. They are in most cases small, at least smaller than the existing agrocombinats, and more flexible. They probably represent the vital future of Macedonian farming.

### *Investing in full-time farms or in part-time farms*

All over the world, part-time farming is increasing and is nowadays the dominant type of farming. That is, however, not in conflict with social efficiency for two reasons. One is that it is hard to organize a seasonal activity like farming in a way offering full-time occupation the whole year around for the involved persons. The other reason is that the social opportunity cost of the labor input seems to be smaller in part-time farming. Even if a growing share of agricultural production takes place in relatively large farming units in most western countries, part-time farmers increase their share of the farming population.

### *Investing in owner-operated farms or in farms based on tenancy*

In an economy short of capital, tenancy may be a convenient alternative to farming based on owner-operated farms. In fact, actors on the market for land should be free to choose whether to buy or lease the farmland. It could be efficient to distinguish the owning from the operating, as usually is done in other sectors of the economy, e.g. housing. It is up to the legislators to efficiently protect property and user rights, irrespective of whether it concerns ownership or tenancy.

### *Investing in expansion of production or in marketing activities*

As the market should be demand driven, it is important to facilitate consumer signaling to producers. In Macedonia there seems to be deficits in price formation, as well as in marketing and trading capacities. Therefore, the main problem now does not seem to be to expand agricultural production, rather to improve the marketing capacity. Improved marketing capacity may eventually lead to increased production, but enhanced marketing should come first.

### *Investing in trading skills or in farmer education*

From the preceding paragraph it seems obvious that trading skills and marketing facilities represent bottlenecks to development, not necessarily education to raise farmer production capacity per se.

#### *Investing in labor-intensive production or in advanced technology farming*

From a social point of view, the present price structure, the high unemployment rates and the productivity indicators, favor a labor-intensive agricultural production.

#### *Investing in an advanced production technology or in farmer education*

As in the preceding paragraph, present circumstances should favor education of small-scale farmers and not investments in advanced primary production technology.

#### *Investing in animals, vegetables, fruits or cereals, etc, production*

Rather than investing in capital demanding commodities, Macedonia should favor the production of labor and land intensive, and capital extensive, agricultural commodities.

#### *Diversify or specialize farm production*

In a labor and land intensive farming, gains from specialization are limited. From the individual farmer's point of view, diversification also may be favorable from a risk perspective.

#### *Borrow and invest or save and invest*

The present price, risk and institutional structure does not favor investment based on borrowing. Even if it is a time-consuming process, investing through internally raised savings may be preferred, being less costly and less risky.

#### *Processing and marketing through farmer owned co-operatives or private firms*

The best case is a hard competition between different organizational forms. However, as marketing of farmer produce might be exploited by local monopsonism, farmer run cooperatives might be (private as well as socially) preferred to the private marketing firms, and this is something for the market to determine. Policy should alleviate the competition amongst organizational forms by setting up appropriate legislation.

## **Conclusions**

At present, Macedonia seems to have comparative disadvantages in its main agricultural commodities, implying that Macedonia might be a natural net importer of food. The competitive part of its agriculture seems to be the small-scale private family farms, while the big enterprises – the agrocombinats – probably should be

reconstructed. A first step to do so might be to separate agrocombinat primary production from agrocombinat processing and marketing activities.

Macedonia fails in taking full advantage of its comparative advantages in agriculture, consisting of the huge amounts of cheap labor and cheap land. These resources should be used to produce cheap and, at least in a first stage, not very upgraded primary commodities.

The Macedonian agricultural policy seems socially costly, favoring farmers at the cost of consumers and taxpayers. The highest cost is related to the import protection policies. Partly as a result of this, Macedonian agricultural markets perform poorly. Especially problematic is the land market, suffering from vaguely defined property rights.

Macedonia can be said to have no *official* agricultural policy. Even if there are a lot of policy measures in use, they are hard to detect, making the policy not very transparent. The objectives are not clearly stated, having the character of visions, sometimes contradictory, and stated by three different ministries.

The objectives about subsidizing exports and taxing imports, i.e. creating trade barriers, may possibly be justified by the “infant industry argument”. That argument for trade barriers is, however, questionable and the policy must anyhow end up in a final abolition of the barriers, in order to be able to reap the benefits from an international competitive industry. Also, the objectives to protect Macedonia from “unfair competition” and “unnecessary imports which could unjustifiably burden the foreign trade balance”, suffer from the same weaknesses. Most probably, boarder protection of these kinds end up in the opposite, namely lost international competition and higher burdens on trade balances.

From a food sector point of view, Macedonia loses from joining the EU compared to a free trade scenario. The main reason is that the CAP will raise food prices above world market levels. On the other hand, Macedonia gains from joining the EU compared to continuing with the present high price agricultural policy in Macedonia.



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