20 years of transition in the agri-food sector

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Prior to 1989 the world could be divided “economically” into three clusters: (1) The Eastern Bloc with its socialist, planned economies, (2) the Western Bloc with its more market-oriented systems, and (3) the developing and emerging countries. Then, at approximately the same time, some major political events took place which contributed to the collapse of the Eastern Block, for example the 1985 elections of the Soviet Parliament, which have been linked to the terms ‘Perestroika’, ‘Glasnost’, and ‘Demokratisaziya’; the East German refugee camp in the German Embassy in Prague in September 1989; and last but not least the fall of the Berlin Wall. Thus came the beginning of the transition process from planned towards market economies in the former states of the Soviet Union (FSU) and Central and Eastern Europe (CEE).

The challenges of transition were formidable. Private and public market-oriented institutions were absent and historical trading paths were interrupted. Many state-owned enterprises collapsed, the private sector was underdeveloped and the market organisations, as well as the producers and processors involved in the agri-food markets, did not know the rules of the “market” game. These issues led to deep and lasting economic distortions.

Twenty years into the transformation of the agri-food sector in the approximately 30 countries that made up the former Eastern Bloc, it is time to recall the inherent changes that have occurred. Our introduction, but particularly the other contributions in this special issue on “20 years of transition in the agri-food sector – analyses of markets and policies” of the Agrarwirtschaft (vol. 58 with numbers 7 and 8), all serve as a platform to review the situation in the agri-food sector in light of the relatively heterogeneous country settings with regard to initial markets, policy and other institutions, as well as the subsequent driving forces of the transition process.

1. The ‘communist’ past and initial conditions

From a ‘western’ economic perspective, the agri-food sector of the former Eastern Bloc seemed organised in a coherent way. In reality, the Eastern Bloc countries had heterogeneous pre-reform characteristics. Countries differed in terms of the “length of time that the communist system [had] existed and the extent to which it was applied, in the distortions of the trade system and the forced integration with other communist countries, and in the level of economic development” (SWINNEN, 2007a: 19). Another differentiating feature “was the capital stock, the technology used in the farms, and the extent of the industrialisation of the agri-food chain” (ibid.). Thus, the initial conditions, including these systematic distortions, were quite heterogeneous. MACOURS and SWINNEN (2000) argue, however, that CEE countries, for instance Hungary, Czech Republic and Slovakia, were ranked at a lower level of initial distortions, while FSU countries such as Russia, Belarus and Ukraine encountered more severe distortions.

Also with regard to the farming structure, tremendous differences existed. For instance, in the FSU or in Czechoslovakia, large farm structures (co-operatives or state-owned farms) dominated. Other countries such as Poland or Slovenia have been traditionally dominated by individual and rather small-scale farming. The differences in initial factor endowment and productivity, as well as the structure of the agri-food sector, in combination with political medium-term objectives, affected the choice of reforms. Today, the region presents itself in a very heterogeneous way with regard to structure and performance of the agri-food sectors.

Overall, five important reform areas in the agri-food sector can be identified (CSÁKI, 2008). These are: (1) macroeconomic and institutional reforms, particularly price liberalisation and subsidy cuts, (2) land privatisation and the reform of related organisations, (3) privatisation and modernisation of the agro-processing and food retail chain (value chain), (4) implementation of operational organisations related to the agri-food sector, and the (5) rural financial market. In the following, these reform areas are revisited and discussed.

2. Macroeconomic and institutional reforms

The economic, legal and judicial, as well as political adjustment processes, as well as ongoing globalisation, have greatly impacted the agri-food sectors of the FSU and CEE. Already at the beginning of transition, fundamental reforms took place. First and foremost, the culture of setting production targets was dropped. Usually, the macro-economic reforms coincided with price liberalisation and cuts in both producer and consumer subsidies (HARTELL and SWINNEN, 1998). Additionally, reduced foreign demand after the collapse of the Council for Mutual Economic Assistance (CMEA) trading system, falling consumer incomes and a

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2 CME countries comprised Bulgaria, Czechoslovakia, East Germany, Hungary, Poland and Romania.
breakdown of the supply chains and state-owned enterprises, all caused major disruptions and thus a squeeze in investment and output (Swinnen, 2007a). Furthermore, the breakdown of the industrial and, to some degree the agricultural state enterprises in rural regions, resulted in previously unknown high rural unemployment rates (on average 21%) that in many countries lasted until the late 1990s and longer (Koester, 1997; World Bank, 2000).

Currently, the agricultural sector and its marketing chain in the former Eastern Bloc are of much higher importance than in Western European countries. One-third of the approximately 500 million people in the former Eastern Bloc live in rural areas and many of them still depend on the agri-food sector for a living. Nevertheless, in line with overall positive economic development and general reform progress, the share of agriculture in gross domestic product (GDP), as well as those employed in agriculture is decreasing. Because the reforms were quite different regarding speed and depth, today huge differences exist among these countries. In this context, one can speak of four groups: (1) market economy in the “old” new member states, (2) advanced reformers, (3) moderate reformers, and (4) slow reformers (Heath, 2003; Csáki et al., 2006; Csáki, 2008).

In general, one can say that the effective implementation of legislation supporting private entrepreneurial activities, as well as privatisation and decentralisation, have caused a sharp increase of private business activities in all CEE countries. In addition, the prospect of EU accession has created an environment more conducive to reform efforts, foreign investments, and the inflow of technology and know-how. Particularly in those countries at the cusp of EU accession, this prospect drove reforms. This trend could be observed in all economic sectors, not just the agri-food sector (e.g. Csáki et al., 2000; Lerman, 1998 and 1999).

Nevertheless, the privatisation experience in the FSU and CEE suggests that a state’s market-relevant institutions and organisations will tend to be unstable and corrupt so long as the competition for asset ownership remains unresolved among major interest groups. The theoretical and policy response, commonly referred to as the post-Washington Consensus, argued that the state needed to institute firm bases of market regulation and the rule of law prior to privatising entire economies. This institutional critique of markets paved the way for creating path-dependent reform programs tailored to specific countries. However, as the transition process did not allow for sufficient time to achieve this, transition seemed messier than normal politics and economics. Indeed, the sequencing and timing of reforms was often an issue of debate (transition in the FSU is often associated with a big bang while CEE opted more often for a gradual reform strategy). Eventually, institutions and organisations consistent with conventional economic fundamentals evolved once privatisation battles over assets were resolved (Schwartz, 2006).

3 While recommendations for the reform of the Washington Consensus were firmly rooted in traditional economic thinking, the post-Washington Consensus accepted the reasoning of Rodrik (2006), namely that institutions matter, that it is important to identify country-specific constraints, as well as to emphasise market failure and the new role of the State (Koester, 2008).

4 Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia, and Slovenia (NMS-10) entered the EU on 1st of May 2004. Bulgaria and Romania followed on the 1st of January 2007, resulting in the NMS-12.

5 The Special Accession Programme for Agriculture and Rural Development (SAPARD) was created in 1999 as a result of the Agenda 2000 and was implemented from 2000-2006. SAPARD was intended to prepare the EU candidate countries for the CAP, i.e. to help candidate countries to deal with the problems of structural adjustment in their agricultural sectors and rural areas, as well as in the implementation of the acquis communautaire in the CAP and related legislation. For the period of 2007-2013, the respective instruments have been rationalised and renamed as the Instrument for Pre-Accession Assistance (IPA) Thus, IPA offers assistance to countries aspiring to join the EU on the basis of the lessons learnt from previous external assistance and pre-accession instruments. Also, the aim of the IPA is to enhance the efficiency and coherence of aid by means of a single framework.
For CEE farmers, EU membership was both a challenge and an opportunity. On the one hand, farms (operators in agri-food business) in countries which have already joined, or intend to join, the EU have been confronted with considerable changes in the economic and regulatory framework, as well as in market conditions. On the other hand, access to the single market and the various instruments of the CAP under Pillars 1 (direct payments and market support measures) and 2 (measures under the European Agricultural Fund for Rural Development) have opened new possibilities for farmers. The complementarities of the two CAP pillars were further strengthened with the CAP reform of 2003. Thus, one can state that the CAP reflects a policy shift that is called the New Rural Paradigm by the OECD (2006), and which places emphasis on regions rather than sectors, and investments rather than subsidies in rural development policy.

In addition to the agri-rural development measures of the EU under Pillar 2, each member country is formulating a National Rural Development Program (NRDP). The NRDPs must be consistent with Community strategic guidelines, but they may indicate the nationally diversified priorities of action. For the NMS, additional transitional measures have been introduced in Pillar 2. These refer to the support of semi-subsistence agricultural holdings undergoing restructuring and the set-up of producer groups. Romania and Bulgaria, the newest member states, can potentially benefit from these measures until 2013. The objective of these measures is to improve the competitiveness of the agricultural sector by bringing small and semi-subsistence farms into the market (NRDP ROMANIA, 2008). In order to design a meaningful NRDP and to implement the policy measures effectively, the principle of decentralisation of responsibilities needs to be functioning, thus strengthening subsidiarity and partnership. For many NMS in CEE this is still a challenging task (MARQUARDT et al., 2009).

Clearly, the introduction and strengthening of Pillar 2 was a well-received reform of the CAP. However, as for the NMS in CEE, the volume of the decoupled direct payments (notably the Single Payment Scheme which can be applied to area or farm units) under Pillar 1 are not only giving farmers a certain level of financial security but are also more substantial than the financial volume of measures under Pillar 2. Furthermore, the NMS can apply the simplified Single Area Payment Scheme (SAPS) until 2013 or in the case of Bulgaria and Romania even until 2016. Nevertheless, the rather complicated bureaucratic procedures required to obtain the payments under the SAPS are preventing this measure from reaching many smaller farm holders, who are in principle eligible. Here it appears that smaller-scale farms are rather disadvantaged due to their limited management capacity. Another interesting feature of the CAP is the so-called compulsory modulation (see footnote 7), that is, reducing spending on Pillar 1 measures and transferring the funds to be spent on Pillar 2 measures of the CAP. A certain percentage share of the direct payments to bigger farms (those receiving more than 5,000€ of direct payments) is shifted to Pillar 2. Yet, this does not seem to make a significant difference for larger farms. What larger farms lose in Pillar 1, they may gain under Axis 1 “Improving the competitiveness of the agricultural and forestry sector” of Pillar 2 (CSÁKI, 2009; HAPPE et al., 2008; SAHRBACHER et al., 2008).

Given the rather severe incidence of rural poverty and the lagging structural change in the farm sector of many CEE countries, including some of the NMS and the FSU, the question may be raised whether the CAP is sufficient to stimulate sustainable economic growth in the agri-food sector, respectively in the rural economy at large. A consensus is emerging that agri-rural policies alone cannot do the job. Farm exit options must be opened up, either in the sense of rural non-farm employment or via socially secure retirement (FELLMANN and MÖLLERS, 2009). Adequate social safety networks have to be installed; bearing in mind that the state budgets of many transition countries are already stressed to their limits. This challenge calls for a more concerted effort in which the national and international political stakeholders of the agri-food sector, of the economy at large and of the social sector work closely together.

4. Land privatisation and reform of related organisations

The transformation of the agri-food sector was always prominent because one of the major reforms entailed the privatisation of land. The Commonwealth of Independent States (CIS) (and Albania) has adopted the ‘land to tiller’ strategy. This strategy implied that the land was allocated to workers of cooperatives without any payment in an equitable manner. In Russia, Ukraine and Kazakhstan, individuals received paper shares that certified their entitlement to a certain amount of land. Most CEE countries (except Albania) have chosen to restitute the land to former owners. All CEE countries, plus the small CIS countries (Armenia, Georgia, Moldova, and Azerbaijan) allocated physical plots to individuals (CSÁKI et al., 2000; NORTON, 2004). Often, an upper limit for land restitution was installed.

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6 At the Berlin Summit of 1999, the chiefs of state reached a political decision with regard to the so-called Agenda 2000. With Agenda 2000, the development policies for rural regions were upgraded and the so-called Pillar 2 of the CAP was born (Council Regulation (EC) no. 1257/1999). Besides agricultural restructuring, Pillar 2 addresses environmental concerns and the wider needs of rural areas (COMMISSION OF THE EUROPEAN UNION, 2006b).

7 The Luxembourg Agreement on the Mid-Term Review in 2003 resulted in a further decoupling of the direct payments from production, introduced new and stricter cross-compliance rules, which required farmers to respect other, primarily environmental regulations, and kicked off compulsory modulation, that is, reducing spending on Pillar 1 measures and transferring the funds to be spent on Pillar 2 measures of the CAP. Furthermore, in 2005 the European institutions established a single fund for the second pillar of the CAP, the European Fund for Agricultural and Rural Development (EFARD), bringing together all the previous measures. The measures of Pillar 2 are divided into four thematic axes (1 = Improving the competitiveness of the agricultural and forestry sector; 2 = Improving the environment and countryside; 3 = Quality of life in rural areas and diversification of the rural economy; and 4 = LEADER, that is, Links between the rural economy and development actions) with more than 40 policy measures.

8 Farm holdings larger than one hectare are generally eligible to apply for the SAPS. Yet completing the paperwork is still not easily accomplished.
The share system was intended to bring equitable land rights to the population, but it often brought about large-scale integrated farm structures and cooperatives (legal persons). Radical changes with regard to land tenure have been carried out in very few countries of the FSU. This is the case for Armenia, Georgia, and the Kyrgyz Republic, where independent private farming now dominates. In Uzbekistan and Tajikistan, private ownership of land is still prohibited by the constitution (Csáki, 2008).

Where land was privatised, it was not so much driven by economic concerns, although theoretical considerations of land and labour productivity may have been considered. This privatisation process was rather prompted by a general sense of justice and had unintended effects in terms of land use changes and farm structures (Sikor, 2009). Politics was willing to pay the economic price: an often-lamented dominance of small farm structures, a varied mix of small and large farm holdings, usually termed dualistic farm structure, or even land abandonment.

Land consolidation is ongoing and is a critical issue for productivity gains. The legal settlement of land ownership relations is also not yet complete, and the establishment of land registries and the emergence of a land market remain priority areas for further reform, especially in the FSU.

5. Reform of the rural financial market

The successful reform of financial systems in the FSU and CEE was of fundamental importance to the economic transition of these regions. The financial intermediaries that the transition countries inherited from the central planning era were not suited, however, to manage modern financial intermediation. In many transition countries, the development of the financial system has continued to suffer – at least in the 1990s – from serious problems: (i) banks continued to finance loss-making, state-owned enterprises (SOE), most notably in agriculture; and (ii) they carried forward large bad loan portfolios and did not effectively control corporate governance and policy. Government mandated lending was the predominant agricultural finance mechanism at the beginning of transition. A variety of funds and credit delivery mechanisms were used to provide the agricultural sector with low-cost credit, where the principal and interest rates were both subsidised. A widespread – and probably correct – view maintains that the beneficiaries of these cheap funds were a special class of borrowers, notably state-owned farms, large-scale borrowers, and clients with strong lobbying powers and close ties to the banking system. Smaller-scale farms, particularly private family farms, were often rationed out. The newly-established credit market in transition countries had difficulties dealing with this new class of privately-owned smaller-scale enter-

9 During central planning, a single bank carried out the functions of both central and commercial banking. The monobank system was typically supplemented by specialised banks, including a national savings bank, a foreign exchange bank, and an agricultural development bank. At the outset of transition, the monobank system was dismantled and the former specialised banks were restructured and often privatised to operate as universal commercial banks (Davis and Hare, 1997). A two-tiered banking system was formally established in most transition countries during the first half of the 1990s.

prises because it lacked experience in assigning a value to assets, especially as the markets for traditional securities such as land and realty were not fully functioning (Heidhues et al., 1998; Petrick, 2004). Credit channelled through the integrator system, where access is linked to output marketing through a marketing integrator, is difficult to quantify but certainly important as farmers still have problems to access the commercial banking sector. In quite a number of the transition countries, especially in CEE, credit co-operatives10 have survived the socialist era. Their savings mobilisation and credit extension capabilities, however, were and often still are limited by the extremely constraining co-operative and banking regulations. For instance, Bulgaria still has not resolved whether or not credit co-operatives should be allowed to collect savings from their members, nor how to integrate the credit co-operatives into the financial system with regard to supervision through the Bulgarian National Bank.

A lack of agri-rural financing continues to be one of the most serious constraints to growth in the agri-food sector, and to growth in the rural private economic sector in general. In CEE, the financing of agriculture has considerably improved since the second half of the 1990s. The creation of a rural banking network has been progressing. While commercial banks play a second-order role as credit intermediaries (they are more important as collectors of savings) in this network, credit co-operatives and, more and more, micro-banking intermediaries are becoming active in rural credit provision (Buchenrieder, 2002). In the great majority of the FSU, however, the rural financial system is not yet fully adjusted to the needs of a market-based privatised agricultural sector. The beginnings of agricultural credit co-operative systems are emerging in those countries most advanced in the transformation of the agri-food sector, namely Armenia, Georgia and recently Moldova (Csáki, 2008).

6. Structure of agricultural production as an outcome of the transition process

The agricultural sectors in quite a number of transition countries are still a mixture of small-scale – even household (subsistence) – production systems and large-scale farming, with three land and animal tenure patterns standing out: (1) large-scale-farming-dominated structures (e.g. the Czech Republic), in which large-scale farms cultivate most agricultural land and/or hold the majority of livestock units, (2) mixed farming structures (e.g. Hungary), and (3) predominately small-scale farming, which is especially the case in the Croatian or Romanian dairy sector. Csáki (2009) estimates that there exist about 30 million small, predominately subsistence farms (0.5–1 ha or less than 1 ESU)11 in the FSU and CEE. Not all reasons for these farms’ persistence

10 It may be noted here, however, that the term co-operative is still very unpopular in transition countries due to their former political mandate during central planning.

11 A more recent development in the EU is the measurement of farm size in European Size Units (ESU). The value of one ESU is defined as a fixed number of EUR/ECU of Farm Gross Margin (FGM). Currently, one ESU equals 1,200 €. Based on this measure, more than 60% of the farms in the NMS in CEE are subsistence farms (smaller than 1 ESU).
are understood yet, but it is generally agreed that such households were important for providing food and shelter during the economic disruptions of the transition period for both resident families and even their urban-based relatives. Additionally, some studies on efficiency and flexibility carried out for Polish agriculture indicate that small farms enjoy advantages irrespective of their size (HOCKMANN et al., 2007, RENNER et al., 2009). Thus, small farms might benefit from their flexibility, i.e., their ability to respond quickly to the dynamic environment (dynamic efficiency), whereas relatively large farms are likely to benefit from economies of scale in purchasing, producing and marketing operations, as well as from positive effects from innovations (static efficiency).

There is an ongoing debate about what could prompt subsistence and semi-subsistence farms (often defined as 1-4 ESU, more than 25% in NMS) to intensify farming, diversify income creating activities, or exit farming; these would foster structural change (with regard to farm size in hectares and ESU) in the agricultural sector and the rural economy at large. A general consensus seems to be emerging that agri-rural development policies alone may not suffice to prompt structural change (see section 3).

Similar to the EU-15, part-time farming plays an important role in transition economies (above 80% of farms in EUROSTAT). Most studies consider part-time farming as a first step out of agriculture, i.e., a high share of part-time farming goes hand in hand with diversification and pluriactivity, and may lead eventually to increasing farm exits. However, there is also evidence that part-time farming and non-farm diversification can be a stabilising factor of employment (BUCHENRIEDER, 2005; BOINEC et al., 2003; MÖLLERS et al., 2008). Non-farm diversification tends to absorb underemployed farm household labour (and thereby reduces hidden unemployment). Clearly, non-farm employment is not a phenomenon of small or large farms. It seems that any size category is somehow engaged in non-farm employment. Nevertheless, non-farm employment may be more important for smaller farms, as the share of non-farm employment income of total farm income can be relatively substantial, which can act as a risk-balancing mechanism (BUCHENRIEDER, 2005). This assumption is confirmed by results from smaller sectoral surveys in transition countries. These results point to a high share of non-farm income in total rural incomes, a figure which varies from 15-68% (BUCHENRIEDER and WEGENER, 2008). DAVIS et al. (2009) confirm this estimate and put a global figure of non-farm income at approximately 58% of total rural income.

In dynamically changing market conditions, the relatively small firms (e.g. farmers, processors) are usually disadvantaged regarding access to input and output markets. In general, small farms use simple technologies, have a low degree of mechanisation, and usually have no assets. Furthermore, because they seem to constitute a high risk and because of their lack of traditional collateral, commercial banks avoid lending to them (HEIDHUES and SCHRIEDER, 2000; PETRICK, 2004). However, farmers need affordable access to various production factors and input and output services to upgrade production technology. As HAZELL et al. (2007: 23) indicated: “If one element of the set is missing, then investments in all the others will be lost or significantly reduced.” Moreover, the advanced age, traditional orientation, and lack of human capital of many smallholders results in limited capabilities to adapt to changing market conditions and to meet increasing quality standards (FRITZSCH et al., 2008, MOLLERS et al., 2009). Smallholders are rarely organised in associations, which also contributes to their low market power and degree of political influence (WOLZ et al., 2006; MARKELOVA et al., 2009). Furthermore, land sale and rental market imperfections combined with land fragmentation, the dualistic farm structure, and missing farm exit options (CIAIAN and SWINNEN, 2006; MOLLERS et al., 2009) impede overall structural change. Another facet of the transformation of the agri-food sector is the diversity of organisational forms that have emerged. Originally, the expectation was that land privatisation processes, especially the restitution process (often with upper limits) would lead to a large number of smaller to medium-sized farms similar to the Western European system (EU BULLETIN, 1999). To some extent this expectation was fulfilled. In a great number of countries (for instance Albania, Bulgaria, Croatia, Latvia, Lithuania, and Romania) individual farms (natural persons) and farm households prevail. However, in some countries that were traditionally characterised by the existence of many small family farms (e.g., Poland and Slovenia), 20 years on the same structure persists. Cooperative structures are widespread in Czech Republic, Estonia, Hungary and Slovakia. By the end of the 1990s, the existence of large vertically and horizontally integrated business groups in the agri-food sector in some countries of the FSU became internationally recognised. Such structures, which are termed agriholdings, are rarely found in the market economies of the former Western Bloc. In the most extreme cases, these mega-agri-businesses can encompass up to one million hectares of land and they also control processing and trade (WANDEL, 2009). Such structures are found, for instance, in Kazakhstan, Russia or the Ukraine. Despite this great variety of organisational forms in farm structures, a gradual increase in average farm size can be observed. This is particularly true for full-time farm enterprises in the NMS. Furthermore, although the number of the larger farms in terms of ESU is relatively small in the NMS, they significantly contribute to overall standard gross margin (SGM). In Bulgaria, for instance, farms larger than 40 ESU (0.6% of farms in EUROSTAT, 2007) contribute almost 50% to SGM. In Romania, 0.1% of the farms (>40 ESU) produce 15% of SGM. At the same time, the number of middle-sized farms (e.g. in Romania) is declining. Hence, a polarisation in production structures, that is, the often-quoted dual farm structure, can be observed (JUVANČIĆ, 2007).

7. Changes along the value chain

Since the beginnings of the transition process, it is generally observable that due to rising levels of average disposable income and increasing urbanisation, combined with changing diets, the demand for processed, high value food products has increased significantly (e.g. SWINNEN, 2007b). Due to these developments, the agri-food market in transition countries have become attractive to foreign companies at all stages of the value chain (retailing, processing, farm and farm input provider). The supermarket revolution that
started in the 1990s in developing countries gained momentum in transition countries as well. In the context of internationalisation, it can be observed that Western retailers and processors bring their own business models to the new markets (FULPONI, 2006; HENSON and REARDON, 2005; PALMER, 2005; ROBERTS, 2005; REARDON, 2007 and 2008). The diffusion of Western quality standards and business models influences the markets of the FSU and CEE at many levels. For instance, in the retail sector this means that traditional, local, store-by-store procurement must be shifted to centralised, large, and modern distribution centres, and external specialised logistic firms must be used (DRIES et al., 2004). The requirements of the newly-established procurement systems demand that suppliers are able to guarantee both disruption-free product flows and the delivery of products of a certain quality. Thus, domestic producers must keep up with quantity and quality expectations.

Since at the beginning of the transition process relationships along the food chain—from farm suppliers to retailers—broke down, new forms of vertical coordination had to be created to overcome problems of insufficient supply and inferior quality. Empirical evidence indicates that due to transition-specific development and various market failures, highly diversified modes of vertical coordination exist in the FSU and CEE, e.g. from almost spot-market transactions over contracting to vertical integration (ANDERSON and SWINNEN, 2008; WORLD BANK, 2005a). Furthermore, contracts can strongly vary in control allocated and risk transferred across stages. Considering the procurement stage, contracts may include farm management assistance, extension services, quality controls, farm input assistance programs, trade credit, and even bank loan guarantees (WORLD BANK, 2005a and 2005b). These programs generate important improvements in the credit situation of the farms, as they contribute directly by improving access to finance (e.g. through trade credit), and indirectly by improving contracting farms’ access to loans from banks or external financial institutions (through loan guarantees, enhanced farm profitability, and improved future cash flows). Several studies (ANDERSON and SWINNEN, 2008; GORTON et al., 2003; WORLD BANK, 2005a) on the effects of foreign direct investments (FDI) in CEE show that foreign investors work hard to raise the level of quality of their suppliers in order to meet their own global quality requirements. Furthermore, international retailers impose high (global) private standards to differentiate their products from those of the competitors, i.e., these standards work as strategic tools (DRIES and KOJAKOVIC, 2004; REARDON, 2007 and 2008). Because the commodities are often produced by households, processors and retailers face quality problems. A leading solution is exemplified by the dairy sector, where processors deal with this situation by both organising their own collecting stations in order to coordinate their suppliers, and by conducting random quality tests. Furthermore, milk processors assure quality supplies from agricultural enterprises by leasing them cooling tanks as part of their contracts. These findings correspond to those of other authors on processors’ farm assistance in other transition countries and sectors, e.g. GORTON et al. (2006) in Moldova, SWINNEN (2005) in Bulgaria and Romania, and HANF and PIENIADZ (2007) in Poland.

However, existing contracts are broken quite often to gain a short-term advantage. One reason for this is that contracts cannot be realised due to poor contract enforcement mechanisms. GORTON et al. (2003) report that medium-sized processing enterprises suffer most of all, with approximately 12% of existing contracts not being realised by suppliers in 2001. At the same time, small enterprises do not use any contracts at all. There are two reasons for breaching contracts in transition countries: First, producers mistrust their buyers and are afraid of not being paid for their production. Second, producers may not be able to fulfill a contract because they cannot access basic production factors (GOW and SWINNEN, 1998). Furthermore, in a WORLD BANK study (2005a), the problem of enforcing contracts was regarded as one of the most important barriers to successful vertical coordination. Indeed, in some cases public enforcement institutions are not fully functioning. Moreover, since transition countries are often described as having limited social capital, there is also an absence of societal enforcement mechanisms (e.g. peer or community pressure, a sense of mutual obligation, and an overall sense of distrust).

However, one has to take into account that, on average, only 40% of total disposable income is available in transition countries’ rural regions (CSÁKI, 2009). For this reason, there is also a high demand for lower quality food. The result is that in transition countries we still find a very heterogenous food demand, meaning that there is a demand for: (a) branded products (high quality and variety, on a global and regional scale), (b) generic products (cheap, because price remains important), and (c) ‘grey market’ products. In countries with high value added tax and ineffective quality control (for instance, Romania and Bulgaria), the gray market still accounts for roughly one-third of total sales volume in agribusiness.

8. Conclusions

Twenty years have passed since the transition process began in the former Eastern Bloc countries. Today we can observe that tremendous overall achievements have been made and overall positive developments can be recognised. The biggest progress has certainly been achieved in price and market liberalisation. However, because great differences existed between countries at their respective starting points, developments have been much more diversified than originally expected. But even if some countries (e.g. Poland or Hungary) can today be labelled as transited countries, some transition-specific problems persist.

The legal settlement of land ownership relations is not yet completed, and the establishment of land registries and the emergence of a sale market for land remain priority areas for further reform, especially in the FSU. Moreover, land consolidation is ongoing and a critical issue for productivity gains in the agricultural sector. Furthermore, secure land rights and functioning markets are closely related to effective rural financial intermediation. Overall, the financial system in CEE and to a large degree in the FSU has been successfully transformed. However, financial intermediation in the rural economy at large, and particularly for the agri-food sector, is still underdeveloped. The commercial banking sector does not want to carry the perceived risk with financing, particularly private, smaller-scale family farms. Nevertheless, alternative financial intermediaries are stepping in; first and foremost credit co-operatives, but also...
so-called microcredit intermediaries. Given the large proportion of people still dependent on the agri-food sector for a living, and the sometimes limited services of these financial intermediaries, however, it is evident that they cannot fully substitute for the commercial banking sector, let alone rural and agricultural insurance providers.

Often the question is raised whether the CAP, even with its more recent reforms, is working for the NMS. This is especially the case with regard to the SAP scheme of Pillar 1, which seems not to work well for very small farm holdings. Pillar 2 measures are more flexible in the sense that the national rural development plans facilitate their adaption specific national reform paths. However, this calls for decentralisation of responsibilities and this political culture still requires time to develop in some of the NMS.

The majority of the counties in the FSU, as well as many eastern NMS, still suffer from glaring patterns of economic disparity. Often it seems as if the rural population is the loser of transition – although there do exist rural regions with substantial economic growth. Low farm incomes are certainly associated with a generally low efficiency of agricultural production (low factor productivity and quality of raw materials) as well as relatively low competitiveness of the entire supply chains. Restricted access to and effectiveness of the administrative service chain is further slowing down restructuring needs of the agri-food sector. Especially for the eastern NMS of the EU, which apply the CAP, the question arises thus, whether the policy measures of the two pillars are sufficient to stimulate broad-scale restructuring needs of the agri-food sector. Moreover, the NMS should be able to build on the institutional heritage of the socialist period to facilitate the transition.

To conclude, the transition countries have taken various developmental paths, this came to many as a surprise. Although some countries may be labelled fully transited by now, many still have to cope with transition specific problems. Many of these problems are associated to the agri-food sector. Thus, the need for developing transition-specific theories (also with regard to the agri-food sector) still exists.

References


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