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1 General review

1.1 Major agricultural market developments in 2005

During the last year (2005), excluding the phenomenon of bird flu, there were no changes or events that had a significant impact on the development of Croatian agricultural market. Since the impact of bird flu is generally well known, in this report we tried to focus our attention to two events that happened in 2005, whose consequences for the agriculture will be evident in the following years.

The opening of Accession talks between Croatia and the EU and Croatia's record imports of agricultural and food products were the most important events in 2005. Complete liberalisation of the Croatian market for EU entry will bring great problems for domestic agricultural producers, especially the small and medium size family farms, because they are not competitive with European producers. However pre-Accession funds have been made available to help the adjustment of domestic agricultural production and the development of rural areas. Beside these financial aids, Croatia will also receive technical support for the development of agricultural policy, agricultural extension services and for the revitalisation of the rural areas. These measures should improve the competitiveness of domestic agricultural production and help small farmers to adjust to the lost profit in agricultural production.

2005 saw record imports of agricultural and food products with imports of 1.30 billion euro and agri-food exports amounting to 743 million euro. Per capita the Republic of Croatia has become one of the biggest importers of food in Europe (300.3 euro per capita) and in the world.

Croatia has large deficits for almost all primary agricultural products, except corn (+7.4 million euro), tangerines (+529 thousand euro) and horses (380 thousands euro). Exports increased for the following agricultural products: tobacco, sugar, food complements, fermented milk products and processed meat. However, a major part of the profitable processing industry is based on imported raw materials, so again there is no profit for domestic agricultural production. It could be expected that some processing industries will move to countries of origin of raw materials.

Small and medium sized farms are the most affected by the import because they generate most of their income from primary agriculture production (having only a small share in processing and distribution). Some of these farms have reduced production, some have completely abandoned agriculture, and what is most troubling many young people of working age have left the rural areas. On the other hand, the increase in imports has enlarged and enriched the food supply whilst slightly reducing the retail prices.

1.2 Agricultural and rural policy developments

In 2002 the new Law of state support in agriculture, fisheries and forestry was introduced. According to this Law state support is composed of two main parts: model of production support and structural measures composed of income support model, capital investments model and model of rural development. Income support model is reserved for non-commercial agricultural producers, whilst commercial producers can use production support and capital investments support. Rural development model is composed of three measures: development of rural area, preservation of autochthonous and protected breeds and marketing preparation of agricultural products.

In 2003 the state support for agriculture, fisheries and forestry accounted to about 90% of total agricultural budget. 95% of this sum was spent on subsidies and only 5% on structural measures.

In order to improve agricultural financing and to lower interest rates, the state gives non-refundable grants to farmers for capital investment in agriculture. The share of investment support can come up to 25% from total value of credit, but not more than 20% from total value of investment itself. Furthermore, support has been arranged for the small farms which are not competitive in the market to ensure a higher living standard for these households. However, due to small amounts of money and very strict conditions (giving up commercial agricultural production) this measure has not been taken up widely.

To reduce the impact of extreme weather conditions, a measure of co-financing the cost insurance premium by 25 % (non-refundable) has been introduced.

The measures for the development of rural areas include the encouragement to seek employment outside agriculture (tourism, services in agriculture, e-commerce and different crafts), the development of rural, hunting and fishing tourism, professional support for the development of rural areas, the development of physical and social infrastructure and the improvement of professional education of rural population. Sadly, these measures are not being implemented because of inefficient administration although they are legally available and there are budget funds for them.

In the last two years, several programs of financing have been launched to promote and increase production of agricultural products in which the country is less than self-sufficient: programmes for permanent plantations and for the development of beef production and vegetables production. Due to many administrative obstacles, such as discouraging the construction of new livestock housing in villages, these measures have had little impact.

1.3 Issues related to the enlargement

The biggest problems will arise concerning the harmonisation of domestic price and market policies, especially direct production incentives. For example, Croatia still has direct incentives for milk production which keep the milk price at a very high level, the highest in Europe and these prices do not reflect milk quality. Removing these direct incentives, means milk production in Croatia will become less profitable and the majority of small producers (1-3 cows) are likely to go out of business. This can cause social problems because the income from milk sales is one of the most important sources of income for small family farms in Croatia.

Problems are expected because of reductions in the aggregate level of incentives and incentives for different products, which arises from the obligations taken by joining the WTO and Accession talks with EU. For example, the reduction of incentives per hectare combined with the reduction of guaranteed price of wheat and no import tariffs will lead to decrease in the competitiveness of domestic production, especially on small farms. Wheat, as well as milk is one of the socially sensitive products in domestic agriculture.

There may be some problems with harmonising policies on rural development. Croatia has formally introduced measures similar to the ones in the EU. However, there are no mechanisms for their implementation, so they have practically no effect on the income in the rural areas. Another problem is how to activate local population in rural revitalisation, cooperation and development of cultural life. Croatia's rural population is passive, poorly educated and with low self-esteem and belief in their own capabilities.

Domestic agricultural production is not competitive compared to European agriculture. The basic reasons for that are small farms, small scale of production as well as technological problems of domestic agriculture. The biggest problems are expected in the conventional production of milk, meat, eggs, fruit, vegetables, wine and wheat. The food industry will also lose a share of the domestic market, especially the producers of meat and milk processed goods, processed fruit and vegetables and confectionary. Producers of traditional farm specialties (kulen, prosciutto, cheese, fruit distillates, olive oil...), direct marketers and rural tourism farms could have significant advantages from their activities. Due to the usage of European funds for rural development, an increase of investments in non-agricultural activities in rural area is expected such as green energy and social services.

Unfortunately, domestic agricultural policies are not taking the necessary measures to prepare those sectors that are under risk on EU Accession; indeed the sectors that could be most adversely affected by market liberalisation have yet to be identified. Hence measures of agricultural policy are being created and implemented without adequate forethought, being influenced by politics rather than the real needs of domestic agriculture.

2 Assessment and outlook: market integration in the cereal sector

2.1 Introduction

The description of the sector (Introduction)

The production of cereals takes up 66% total arable surface in Croatia. Maize is planted on some 400000 hectares which is 55% of the cereals area. Maize production in 2004 was 2.15 million tonnes with average yield of 5.3 t/ha.

The area of wheat has reduced from 240 to 200 thousand hectares over the past five years, with wheat production normally fluctuating between 0.95 and 1 million tonnes per year with average yields of 4 t/ha. However, in 2003 abnormally bad weather caused the average yield to fall to 3 t/ha. The Ministry of Agriculture wants to reduce area under wheat to 100000 hectares because of the expensive support they are providing for wheat production.

The production of barley takes up about 50 thousand hectares (7% of surface under cereals). Production fluctuates between 160 and 180 thousand tonnes, and yields from 2.5 to 3 t/ha.

Oat is produced on 20 thousand hectares, total production being 50 thousand tonnes and yield of 2.7 t/ha.

In 2003 the production and yields were 40% smaller than average because of extremely bad weather conditions.

In the overall production of cereals farms contribute 80% and companies 20%. Compared to companies, farmers have a lower level of technology and have smaller yields.

In 2005, the foreign trade deficit in cereals was around 12 million euro. Deficit in exchange in 2005 for wheat was 6.6 million euro, for barley 7.1 million euro and for oat 56.6 thousand euro. There is a positive balance in exchange of maize, 7.4 million euro in 2005.

2.2 Expert views on infrastructure (storage facilities and transport)

Wheat for human consumption is stored in silos and floor storages. Corn is mostly stored on the farms, attics and corn baskets. Barley and oats are also stored on the farms.

There are many different storage facilities in Croatia, but since they are not adequately tracked we can only estimate their number and size. The number of silos and storage facilities is estimated to around 70. The volume of storage facilities for wheat is estimated to 1.8 million tonnes of which the capacity of silos is about 1.6 million tonnes, and capacities of floor storages about 258000 tonnes. In the last ten years, smaller silos are built on farms with capacity from 500 to 5000 tonnes.

Present storage capacities meet only half of the needs for storage. It must be noted that current storage facilities are mostly run-down, especially in eastern Slavonia, and their equipment is outdated, 15 do 40 years old.

One of the main problems of domestic cereal market is the issue of ownership of storage facilities. Farms that produce 80% of cereals have no storage facilities and are forced to sell the wheat in the time of harvest when the price is at the lowest level or to pay the service of grain drying and storage.

After harvest, farmers usually transport the wheat in their own tractors to the farm where it is temporarily stored or it is taken immediately to the purchase point. Larger producers also use trucks. For the transport of cereals on the distances larger than 50 km, trucks are usually used (maximum load of 24 tonnes).

2.3 Expert views on quality

The quality of cereals in Croatia is rather low and the annual fluctuations in quality are significant. Lack of modern storage facilities gives rise to quality problems during storage. The standards for maize are maxima of 14 % humidity, 2 % grain fraction, 2% defective grains and 1% additives.

2.4 Expert views on the possible or existing market distortions

Ministry of Agriculture, forestry and water management has set the guaranteed price of wheat in 2005 at level of 0.10 euro/kg. A minimal redemption price is set at 0.12 kn/kg with the incentive of 0.22 euro/ha paid to producers of wheat. State also gives incentives to traders (0.008 euro/kg).

The Croatian wheat price was kept above the world price and prices in the neighbouring countries (100 – 105 euro/ton) by means of a high tariff on wheat and, on several occasions, a ban on import was introduced. Following Croatia's membership of the WTO the tariff barriers on cereals and cereal products are being reduced.

2.5 Assessment of market integration

In accordance with Croatia's WTO obligations and various bilateral agreements including that with the EU, Croatia is liberalising the domestic market for food and agricultural products by reducing tariff barriers. The overall level of support will also be reduced and in 2005 it was 1.3% of Croatian GDP. In the cereals sector production incentives have been replaced by area payments. There has been a growth in foreign trade in agri-food products. The domestic market has also been opened up through the recent entry of foreign food retailers. .

2.6 The usage of mechanisation and inputs in the production:

There are data on mechanisation used by agricultural companies while there are no statistics for family farms. From time to time Ministry of agriculture issues a rough estimate.

It is estimated that Croatia has over 130 thousand tractors and on average there is one tractor per 7.11 hectares of land (2.94 kW/ha) or 5.6 hectares of arable land (3.77 kW/ha). On average, family farms are equipped with 1.4 two axis tractors of average power of 30 kW and average age of 17 years and 0.29 one axis tractors per farm of similar age. The state of agricultural mechanisation is bad as can be judged from the average age.

Most producers, (95%) use certified seed because it is a condition for receiving aid payments. If this stipulation were abolished, it is expected that usage of certified seed would fall below 50% of the total seed.

The usage of artificial fertilizers is relatively low and in combination with low usage of plant protection products results in relatively small wheat yields. It is estimated that only 50% of the optimal amounts of fertilisers is used in the production of wheat, and in the case of maize only 30%.

More than 90% of producers use herbicides but only 20-25% spray against pests and diseases.

2.7 Conclusion

In the coming years, the wheat area payment and wheat price supports are expected to be gradually reduced resulting in a fall in wheat area and volume of production. Maize production will probably increase while the production of other grain crops will stay at approximately the same level.

After the formation of the free trade zone of western Balkan countries or reformed CEFTA agreement, larger imports of wheat and barley from Serbia are expected, this could lead to major problems for Croatian grain producers. Along with economic and social problems, there could be crop rotation problems especially for growers of industrial herbs.