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MONITORING OF AGRICULTURAL POLICY, MARKET AND TRADE DEVELOPMENTS IN CYPRUS

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The project aims to establish a network of experts involved in agricultural policy analysis and rural development in the New Member States, in the Acceding Candidate Countries and in the countries of the Western Balkan. More detailed information on the project can be found at www.agripolicy.net.

CONTRIBUTION OF CYPRUS

1. GENERAL REVIEW OF AGRICULTURAL DEVELOPMENTS

1.1. Major Agricultural Market Developments in 2005

Following Accession in May 2004, agricultural markets have been affected in several ways. Below we select and expound on three major changes which affected agriculture in Cyprus in 2005.

- Increase in Production Costs – The case of water
- Abolition of Marketing Boards – The case of potatoes
- Imports displacing local production – The case of fruit and vegetables

1.1.1 Increase in production costs – The case of water

A major and permanent issue in Cyprus' agriculture is water. Cyprus does not enjoy plenty of rain and consecutive years of very little rain are not uncommon. Furthermore, even when rainfall is above average, farmers still rely on water supplied by the Water Development Department of the Ministry of Agriculture. Since Accession there have been important developments/events, both foreseen and unforeseen.

Water was one of the products/services that have long been cross-subsidized between different categories of consumers. This practice has been changing and the price of water for agricultural purposes has seen steep rises. Commencing from about 6.5 cents (Euro 0.114) per metric ton less than 2 years ago, there have been several increases at 7, 8 and 9 cents per ton. The latest increase was at January 1st reaching 10 cents (Euro 0.175) per ton for a total increase of over 50% within the last 20 months. An additional increase to 11 cents is scheduled at 01/01/2007. Although this increase was inevitable due to the issue of cross-subsidization it was not effectively dealt with. Indeed, not many options seem to exist in this area other than to absorb the cost, reduce production or switch to less water-demanding crops.

Other than the foreseen increase in the cost of water, there always seems to be the recurring problem of water availability. Despite its recurring nature, water availability is not easily dealt with. Reservoirs overflowed two years ago – a rare event. They were down to 76% of their capacity at the end of February 2005 and to a mere 48% at the end of February 2006. The Water Development Department decides accordingly as to how much water the farmers get. Two years ago they had been offered 100% of the water they needed, last year that dropped to 80% and is now at a very low 40% of their needs. Water is rationed in favour of permanent crops, so this year permanent crop areas will get 45-50% of their needs, while temporary crops will get a mere 20%.

More expensive water means higher costs of production. Less water means lower production (since some land is left without water), lower quality or often both. In their effort to overcome these problems, some farmers try to draw water from sub earth water reservoirs. This practice has been overdone to the point that all these reservoirs have degraded. In most cases the water degradation range from moderate to severe. To quote an official - “In a few cases the water salt content is approaching that of seawater”. Thus, water is a major and possibly permanent issue for Cyprus’ agriculture that would keep causing fluctuations in quantity, quality and farmers’ income. Both last year and 2006 seem to be among the difficult ones.

1.1.2 Abolition of market Boards – The case of Potatoes

The abolition of the monopoly power of the marketing boards together with the abolition of the direct Government support for the marketing of agricultural products created financial difficulties for producers who were forced to market their products direct or through middlemen.

As a consequence of the difficulties faced by the farmers, Producer Organizations were formed. At least 18 such groups are in existence today. Their major goals were increasing the producers bargaining power and better organization including scheduling and adjusting production according to the market’s needs. Despite the effort and money (funded by 2004-2006 Rural Development Plan) their results are far from perfect. The major obstacles are the staff’s inexperience both in their responsibilities and in the trading in a free market with competition from imports and with no government support. For example, the semi-government Potato Marketing Board had been responsible for the trade of potatoes. Potato growers were annually receiving approximately 10 million Euros as compensation for the low export prices in June and July. Since Accession, potato growers created four Producer Groups for the production and marketing of potatoes. The outcome was

- Export income fell since the four groups were all trying to sell to the same importers
- This decrease was not offset by the subsidies provided by the Rural Development plan. These were far lower than the 10 million euros they had been receiving
- Owing to the abolishment of the monopoly in the import of seed, new varieties are planted and surpluses have begun to appear in the local market – leading to a fall in the prices paid by the local consumers
- On the positive side a new export markets were opened up by the new Groups

Faced with these changes and with street demonstrations, the Cyprus Government opened a dialogue with the growers, hoping to establish a National Plan for potatoes.

As far as consumers are concerned, since Accession they have benefited by paying lower prices and having far more choices for most agricultural products.

1.1.3 Imports displacing local production – The case of fruit and vegetables

Immediately after Accession the Cypriot market was inundated with fruit and vegetable imports from EU countries, mostly from Greece, Italy and Spain, at prices 40% cheaper than the price of similar local products. Despite the fact that the taste* and quality of imported fruits and vegetables –with the exception of apples, pears and bananas- compared poorly with the taste of local products, initially consumers bought imported products. This forced the Cypriot producers to adopt defensive measures that included:

- Better scheduling of harvesting to avoid oversupply and lower prices
- Formation of Producer Organizations through which the producers regulated supply and quality of their products, and at the same time received financial support for their administration expenses (5% of their marketed production for the first and second years) and for their investments in land, buildings and machinery (55% of the cost)
- Increased their exports of vegetables to EU countries

These measures, coupled with the unsatisfactory taste and quality of imported products (e.g. tomatoes, grapes) enabled the producers of fruits and vegetables to maintain their production levels in 2005.

Producers of apples and pears, on the other hand, faced greater difficulties, with their price falling by half due to high quality imports. Worst off were the banana growers who were unable to sell their products and were, therefore, forced to destroy them.

Producers suffered lower incomes and a stimulus for exporting fruit was created. Apple, pear and banana imports will inevitably result in some restructuring of the fruit-growing sector.

* A pre-accession survey had the following findings: Given that local and imported fruits are similarly priced 90% would choose local fruits. Reasons: Better smell/taste 43%, trusting local producers 20%, supporting local producers 14%, other reasons 13%.

1.2 Major Agricultural and Rural Policy Developments in 2005

Following the overwhelming response to the 2004-2006 Rural Development Plan in 2004, when applications for funding equalled 168% of the available funds, the Government approved additional funds for 2005. The original budget of 93m CYP (Euro 162m) was co-funded by Cyprus and the EU had agreed to co-fund the plan with but the additional funds of some 70m CYP (Euro 122m) came solely from the Cyprus government. Again applications greatly exceeded the budget and led to the introduction of stricter criteria for judging applications, but even so not all qualifying applications will be successful. The vast majority of applications have been for the two major axes of the plan: a) improving competitiveness and modernising production and marketing of agricultural products and b) protection and improvement of the environment and strengthening of the socioeconomic conditions of rural areas.

New policies

Formulation of the Rural Development Plan 2007-2013 is underway. The first draft is scheduled to be delivered by April 2006, while the final version will be submitted for EU approval by June 2006. Following the National Strategy the four axes will be:

- Axis 1: Improving the competitiveness of agricultural products
  Focus: Creation and/or transfer of knowledge and know-how

- Axis 2: Improving the environment
  Focus: Protection/enhancement of biodiversity and ecosystems
- Axis 3: Creation of new jobs in rural areas
  Focus: Women and younger people. Aided by: encouraging creation of small businesses, upgrading local infrastructure, encouraging tourism, and promotion of information technology and telecommunications
- Axis 4: Incorporating 'Leader' in rural development
  Focus: Mobilization of people in rural areas for a bottom-up action. Aided by: Creation and continued support of Local Action Teams that would develop their strategy according to their local needs and resources

Among the policy initiatives under consideration within the Ministry of Agriculture are:

- Diversification of agricultural income. (E.g. A horse raising farm could have a riding school or it could offer donkey rides for tourists to the nearby villages).
- Increasing the income of the whole agricultural family (e.g. women in some villages have traditionally produced hand-made tablecloths to sell to tourists)
- Measures for respecting the environment, protecting the consumers' health and protecting the animals' well being
- Conserving the traditional landscape. Coastal areas have lost their traditional identity due to tourism-related developments. The effort will be in conserving the inner areas' cultural identity. Measures will include incentives for young people settling in villages' cultural centers
- Emphasis in the development of Agro-tourism in connection with measures as above
- Emphasis on quality products

In the case of Agri-tourism the effort is being aided by the Cyprus Tourism Organization and the Department of Urban Planning.

A Hectare Subsidy system began in 2004, managed by the Cyprus Organization of Agricultural Payments. Many difficulties and obstacles were encountered leading to the following changes during the 2005 season:

- Restructuring of the organization
- Improving/simplifying procedures
- Specialisation of human resources
- Better information for applicants leading to fewer errors in the applications

The process of payments started in October and was finished by the end of December. A total of 41,473 applications were filled. Applications for 2006 have been accepted since

January 23rd. The deadline is March 24th and payments are scheduled to begin by October 17th.

Other Policies:

An improved Agricultural Insurance Plan was formed. The new plan provided cover for an additional array of circumstances. A further improvement came in the way the premiums were handled.

The building of new water reservoirs has begun. In some cases, the plans call for the re-allotment of properties, construction of new roads and irrigation by pipes instead of streams.

A major problem that increases the cost of production is that of small and scattered properties. An area of 15,000 hectares has been studied and its re-allotment is underway.

1.3 Issues Related to the Enlargement

The transition period for Cyprus has not been easy. Before Accession, it had received very few funds for restructuring its agriculture and agricultural income has been decreasing. The farmers are trying to modernise their machinery as can be seen by the number of applications in the corresponding section of the Rural Development Plan – it is part of Axis 1 which is the most oversubscribed Axis of the Plan. Producers of grains, fruits and vegetables and potato growers face the biggest difficulties which mainly from the abolition of national subsidies following EU-Accession.

As mentioned above, semi-governmental organisations have given way to other organisations that have yet to become experienced and efficient enough in their responsibilities. The farmers themselves have still difficulties in realising their new role in a free and open market. Following decades of government funding, innovation was very low and resources were allocated inefficiently. Many farmers simply refuse to realise that they may not be efficient enough to stay in business and may keep operating at a loss because they believe that the government will eventually help them recuperate their losses.

2. ASSESSMENT AND OUTLOOK: MARKET INTEGRATION IN THE CEREAL SECTOR

2.1 Introduction to the sector

Most of the grain growing areas of Cyprus were lost by the Turkish Invasion in 1974. Since then Cyprus has grown grain on small non-arable farms with annual production varying greatly with the weather.

The two main cereal crops are barley, which is used exclusively for animal feed, and hard wheat, grown on irrigated land, which is used exclusively in flour milling.

The area cultivated with barley and wheat has been the same for the last five years at 52900 hectares of barley and 5900 hectares of wheat. Before Accession the Cypriot cereal producers were heavily subsidised getting a guaranteed price of 250 Euros per tonne for wheat and 220 Euros per tonne for barley. After Accession, in 2005 the Cypriot cereal producers sold their wheat at 150 Euros per tonne and their barley at 120 Euros per tonne. It has been estimated that, with the various support measures included in the Rural Development Plan, producers will have the same income as before. As the support from the Rural Development Plans will decrease in the coming years, cereal producers' incomes will fall. This, together with increasing competition from better quality imported wheat and barley, is likely to induce some farmers to stop producing barley.

However, the total area planted with cereals is not forecast to fall, because other farmers, practicing crop rotation, may plant cereals as an alternative crop.

The production of barley and wheat in Cyprus varies with the weather conditions. For the period 1999 – 2005 the average yearly production was 10639 tonnes of wheat and 111760 tonnes of barley. There was no production of maize or oats.

During the same period the average yearly imports of the various cereals were:

Wheat	86890 tonnes
Barley	317443 tonnes
Maize	215115tonnes
Total	619448 tonnes

The total consumption of the above cereals in Cyprus during the same period averaged 719511 tones yearly and the yearly percentage of imports to total consumption averaged 86.2%. The value of the local production of cereals during the same period averaged 26 million Euros while the value of imported cereals averaged 70 million Euros.

2.2 Expert views on Infrastructure

2.2.1 Storage

In 1954 the Government of Cyprus established the CYPRUS GRAIN COMMISSION (CGC) and gave it monopoly power to:

a) Collect the local production of cereals (barley and wheat) at agreed prices
b) Import the necessary quantities of cereals to satisfy local demand

Until May 2004 the Cyprus Grain Commission delegated the collection of wheat and barley to a cooperative organisation called SEDIS. Grain producers transported all their harvested cereals, other than those retained for on-farm feeding to livestock, to the SEDIS open–air or covered stores. SEDIS has the capacity to store 20000 tonnes of cereals in covered stores and 80000 tonnes in uncovered stores. During the last five years SEDIS doubled its covered storage capacity through the construction of silos.

The CGC has storage capacity in the ports and elsewhere for about 90000 tonnes of imported cereals in silos and another 100000 tonnes in covered stores. Until 2004 the CGC also stored any local production that SEDIS could not store.

After Accession the relationship between CGC and SEDIS ended and SEDIS received the 2004/05 local cereal production and sold it to the users who were animal feeding mills and animal farmers. SEDIS is planning to increase its covered storage areas by converting some of its uncovered area to store another 20000 tonnes.

The CGC storage facilities which are all covered and can store up to 200000 tonnes are of very high quality standards and are continuously under inspection. Cereals are stored at low temperature with good ventilation and air conditioning in order to reduce the heat created by the storage and in order to avoid infestation by insects.

Imported cereals are inspected and chemical analyses are carried out for dioxins and other additives before being unloaded from the ships and stored by the CGC.

CGC now acts as a free trader importing and selling cereals which it imports mainly from EU MS. Traditional importers of animal feedingstuffs and new traders have also been importing cereals since May 2004.

There is evidence that the other importers of cereals are planning to construct silos and covered stores for about 25000 tonnes. Many livestock farmers are doubling their on-farm storage capacity from 2500 tonnes to 5000 tonnes using subsidies (of 50 to 60% of the cost) under the Rural Development Plan 2004 – 2006.

2.2.2 Transportation

Owing to the small distances in Cyprus, transportation costs for cereals are uniform as they relate mostly to the cost of loading and unloading the trucks. The cost of local transport of cereals is 3 Euros per tonne. Since Accession transport costs have increased by more than 40% due to the increase in the price of oil.

2.2.3 Expert views on quality

The quality of local hard wheat is very high. It is produced on irrigated land and the 6000 – 10000 tonnes produced annually are used in bread making. There is no variation in quality from year to year.

The quality of local barley is not constant over time. This is especially true of the barley produced from farm saved seed. In order to improve quality and maintain yields the Ministry of Agriculture authorised the Agricultural Research Institute to experiment with new varieties which are planted experimentally by the Seeds Production Section for cereals of the Ministry of Agriculture, Natural Resources and Environment.

The Seed Production Section for cereals establishment more than 50 years ago, provides the farmers with 80% of their needs for certified barley seed at about 300 Euros a tonne. The emphasis is in producing seed which, when grown, will not have weeds.

In the five years before Accession farmers invested heavily in equipment for cultivation, seed planting, adding fertilisers, spraying with pesticides and harvesting.

After Accession cereal farmers have applied for 2 million Euros of subsidies under the Rural Development Plan for the purchasing machinery and equipment. .

Despite these attempts to improve the quality of locally produced cereals, the inherent negative factors (variable weather, small scattered plots on each farm, no crop rotation, and using farm saved seed) hinder high quality production. On the other hand, imported cereals of consistently high quality are available at competitive prices.

Livestock farmers are prepared to continue to buy local cereals provided their price is at least 20 Euros a tonne lower than imported cereals.

2.3 Expert view on possible market distortion

The market for cereals used for human consumption (almost exclusively hard wheat) has not changed after Accession and is not forecast to change in the near future. It is estimated that the cereals used for human consumption will amount between 95000 and 105000 tonnes bought mainly from the CGC, though one of the leading Cypriot flour mills has started importing wheat for milling from EU countries.

The situation in the animal feed market in Cyprus is completely different after Accession and is characterized by the following.

1. Local producers sell their cereals at 90 Euros a tonne less than before and complain that the subsidies under the Rural Development Plan do not compensate them for that loss. For the next 3 to 5 years as the transition subsidies progressively decline and eventually stop, cereal growers in Cyprus will cease producing as they will not cover their costs. This forecast decline in cereal cultivation might not be so severe if the quality of locally grown barley is improved considerably through the quality improvement program of the Seed Production Section for Cereals and if the productivity of cereal farms is improved with the use of improved machinery and equipment bought with the subsidies of the Rural Development Plan.

2. The animal feed mills that could buy barley before Accession for 80 Euros/tonne and now face a price of about 140 Euros are substituting other raw materials for barley, notably imported feed wheat. .

3. The production of many livestock products in Cyprus including meat products, milk products (especially cheese) will be reduced due to:

    - Competition from cheaper EU origin products
    - Stricter application of hygiene standards (e.g. HACCP) in the production and the selling of food products of animal origin.

    These changes will result in the reduction of the animal population with a consequent reduction in cereals consumption.

4. The marketing of cereals used for animal consumption which in Cyprus was monopolistic before Accession, is now very competitive with such key players as:

    - Private importers who are merchants
    - Animal feeding mills who are now importing directly
    - SEDIS which started importing cereals since May 2004
    - The CGC which was enabled by legislation after Accession to use its storage capacity to play a leading role in cereals trading avoiding, however, using its dominant position.
    - A higher percentage of the locally produced barley will be consumed on the farms or traded between farmers.

Early in 2005 there was a threat of market distortion because the CGC decided not to rent the storage spaces it had to the free traders in order to maintain its monopoly situation. However, with the invention of the Government the CGC agreed to rent storage space at a low rental to any free traders who applied for space.

2.4 Assessment of the Market Integration

Cereal imports from EU countries into Cyprus before Accession represented around 7% of total imports. It is too early to quantify the longer term impact of Accession.

2.5 Input – Output for Cereals

2.5.1 Machinery

Purchases of machinery by cereals farmers have increased since May 2004 due the 50% to 60% subsidies available under the Rural Development Plan 2004 - 2006. It is estimated that about 4 million Euros have been invested by the cereals farmers for the acquisition of tractors and machinery for cultivation, spraying, harvesting and storing. This sudden surge in the demand of machinery led to an increase in prices of 10 to 20%. The purchase of new machinery was mostly for replacing old and outdated machinery and there is no evidence of a substantial increase in mechanisation. The new machinery resulted in reduction in the time and costs of cultivating, seed planting and harvesting with a consequent increase in productivity.

2.5.2 Fertilisers and Pesticides

The use of fertilisers has remained constant over time whilst there was a small decline in the need for herbicides due to planting higher quality weed free seeds. The prices of fertilisers and pesticides are not expected to change relative to the prices of cereals as fertiliser prices are expected to fall.

2.5.3 Price of fuels

The most important factor for the increase of the costs of cereals farmers is the rise in fuel costs. Fortunately the increase in the price of fuel to farmers did not follow the general increase in the price of fuel, because the government provides farmers with heavily subsidised fuel.

2.5.4 Prices of locally produced cereals

Cereals farmers have not been able to pass the increase in costs on the price of cereals, because of the increased competition from imports and consequently they are suffering from declining profitability.

2.6 Outlook for cereals

Cereal Production in Cyprus in 2006, due to the drought, is not expected to exceed 75% of the 2005 level and in late January 2006 the farmers were in despair. Heavy rainfall in early February made them less pessimistic but nevertheless the barley harvest will be about 20% below the average of the past five years. Cereals imports will consequently rise to compensate for the shortfall in local production.

The income of the cereals farmers in 2006 and until 2010 will decline, though the fall will be mitigated by compensating subsidies per hectare under the Rural Development Plan.

In the longer term cereals farmers, faced with low prices for cereals and the reduction and abolition of area subsidies, will have to decide whether to continue growing cereals. The most important factors which will cause a reduction in the area of land cultivated with cereals are the following:

- Prices of cereals
- Increase in the costs of producing cereals
- Reduction of government support measures and subsidies per hectare
- The system of hereditary succession in Cyprus by which parents divide the land to their children and create small farms which are abandoned or rented to professional farmers
- Very few young persons choose farming for living
- Despite the efforts of the Seed Production Section, the quality and protein content of local barley are lower than those of imported barley.

The factors which will slow down the reduction in the area cultivated with cereals are the following:

- Older cereal farmers who have no other income generating activities are likely to continue to grow cereals.
- Cereals farmers will want to utilise the new machinery which they bought from 2004to 2006 with the government subsidies
- Some farmers may rent their land to professional cereals farmers who will thus be able to spread their fixed costs over larger areas.
- Other farmers may rent their lands to livestock farmers who want to grow cereals for their animals.

Some experts anticipate a progressive decline in the volume of imports of the main cereals due to the following factors:

- Substitution of other materials for cereals in animal feedingstuffs.
- Reduction in the local production of meat, poultry and milk which will be replaced by better quality and cheaper products resulting in reduction of cereals imported for feedingstuffs.

On the positive side the longer term prospects of the cereals sector in Cyprus might improve depending on the sector support programmes which are certain to be included in the Rural Development Plan for 2007 – 2013.