

NEW FISCAL ROLE OF THE GOVERNMENT IN THE TRANSITION OF THE AGRICULTURE IN SERBIA

Igor Pejovic¹, Vladimir Jovanovic²

Summary

It is necessary to use huge potentials in agricultural and food processing sector in the Republic of Serbia during the EU accession process. Due to world economic crisis, lack of direct foreign investments, unfavorable conditions in banking sector and irrational usage of available resources, it is necessary to prepare agriculture in order to cope with free competition on the European market. Therefore, there is a need for appropriate support to agricultural development in line with international standards. This requires changes in course of national support to agro-economic development in the fiscal area, or in other words, adoption of number of stimulating financial measures in agrarian policy of the Republic of Serbia.

Key words: *agricultural production, Republic of Serbia, fiscal and agrarian policy, agrarian budget, subsidies, rural development and EU accession.*

JEL: *O13, Q10, E63, E60*

Introduction

In the current economic and financial conditions there are many reasons of economic and financial nature, which determine the necessity of establishing permanent sources of agriculture financing through agrarian budget. Solving of complex development problems in agriculture is impossible without introducing a wide range of tax incentives and exemptions. An orientation towards market liberalization and free international trade is undeniable, but also it is necessary through fiscal policy measures to introduce an effective system of subsidies for agricultural production, as it is a case with developed countries of the European Union. It may be noted that the budgetary resources compared with those in countries from the region and the European Union are insufficient for achieving the existing and development priorities in agriculture. This directly affects the unfavorable

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economic situation and the international competitiveness of agriculture and makes structural adjustments to customs and other requirements of the European Union difficult. At the same time, contemporary agricultural policy means an active agrarian budget directed towards the development of SMEs and entrepreneurship. In today's environment, strong governmental support for rural development and financing of specific agricultural production is insisted on, which requires reform of fiscal forms, which have different effects on agricultural development.

Research methods

The research was conducted using various research methods and techniques like: induction, deduction, analytical and synthetic descriptive method. Contemporary domestic and foreign literature was used in the paper.

Financial government support in agricultural production

Inadequate role of the government is one of the basic problems of agriculture in Serbia in the period of transition and EU accession in the conditions of global economic crisis.³ This is confirmed by the lack of systematic measures of macroeconomic, agrarian and fiscal policies, causing chronic problems that cause unfavorable economic position of agriculture.

In recent years there is a necessity for strong government support in financing of the specific agricultural production. In this context, the agrarian budget should have an important role, because it unites government measures in the field of agriculture development. Financial measures also apply to a variety of fiscal measures, privileged credit investments from primary issues, subsidies for agricultural production and others. Permanent financial support of the state is conditioned by the necessity of investing significant financial resources in agriculture, characterized by a long period of retention and turnover of invested funds and a lack of own funding sources due to low profit margins in primary agricultural production. Taking these specificities into account, in the last decade of the twentieth century, Central Bank directly provided the funds for financing the agricultural production, with privileged interest rates. On the basis of credit policy which acknowledged the seasonal character of a production and the need for short-term investments, a support for agriculture was sought. These selective primary issue credits from commercial banks were based on macro-economic and agrarian goals in a given year. Loans from the primary issue were approved with the discount rates, which were significantly lower than current interest rates on financial markets. During this period, the predominant part of funds from the primary issue was directed to agriculture. Funds from the primary issue invested through selective loans were insufficient and inadequate for agrarian needs, thus, this did not provide a sufficient impact on improving the economic position of agricultural entities. Financing of the agriculture from primary production was abolished in early 1994, because the investments mentioned above contributed to growth of the inflation rate. During this period a need for a new way of financing of the specific agricultural production emerges in the conditions of reduced money supply and rising interest rates of

3 Milanović, M. (2006): *Približavanje Srbije Evropskoj uniji-novije komparacije poljoprivrede i agrarne politike*, Ekonomika poljoprivrede, Beograd, br. 2/2006, str. 96-97.

commercial banks. This has caused the growth of the production costs and the emergence of pronounced financial crisis in the sector. These and other reasons have caused the necessity of establishing permanent sources of funding through the agrarian budget, as a part of the budget of the Republic of Serbia.

The agrarian budget

The funds from the agrarian budget provide support for maintaining of the current production and for an agricultural development. Incentives from the agrarian budget were insufficient to achieve the priorities of the agricultural production modernization, to satisfy the needs for market supplying and to ensure better situation for the agricultural producers⁴. During this period, the average subsidies in agriculture per capita ranged six to eight times less than in the European Union, while expressed per hectare these were about twelve times less than in the EU. It may be noted that agricultural production then had ten times less government support than in the developed countries of the European Union. At the same time, the short and long term goals of the agrarian budget were not accomplished, in terms of increased competition, quality, standard of living, production, exports, productivity, technological innovation and development of rural areas.

The share of agricultural funds in the budget of the Republic of Serbia amounted to 5% to 8.3% during the 1996-2000 period and 3.10% to 6.2% in the period 2001-2006. These funds were insufficient, as evidenced by the data on the share of agriculture in GDP (12.90% to 24%).⁵ During this period, the predominant part of the funds from the agrarian budget included premiums for milk producers (33%), crop production and others. Incentives for village revitalization have been abandoned in 2001 when subsidies for wheat purchasing were introduced. In accordance with development priorities, in 2003 the incentives were introduced for the export of agri-foodstuffs, improving the quality of land and subsidies for the expansion of the estates. Agricultural policy has failed to improve the financial situation of the agriculture in Serbia during the recession.⁶

Changes in agricultural policy, following the example of developed economies, were made in 2004 in order to adapt agricultural production to market economy. Incentives were introduced for agricultural and food products market development, credit financing and rural development. Aimed at increasing of the estates size, the support was given to long-term leasing of agricultural land and the non-refundable financing of the development priorities in agriculture was performed. Premiums for milk were not paid to processors any more but directly to agricultural producers and registered farms. Measures of support to production and market (55%) and to rural development (20.1%) and the costs of public and professional services (24.9%) had the largest share in the agrarian budget in 2004.

4 Cvijanović, D., Pejanović, R., Milanović, M. (2006): *Tranzicija poljoprivrede Republike Srbije - dometi, efekti i ograničenja*, Ekonomika poljoprivrede, Beograd, br. 4/2006, str.938-939.

5 Radović, G. (2009): *Podrška države u funkciji finansiranja poljoprivrede*, Agroekonomika, Beograd, br. 41-42/2009, str.74.

6 Birovljev, J. Glamočanin, B. (2011): *Agrarna i ruralna politika u Srbiji*, DAES, Ekonomski fakultet, Novi Sad, str. 25-39.

Incentive credit policy was introduced in 2005. Funds for abetment of credit policy (20.7%) have increased their own share in the agrarian budget in 2006. The abetment of a rural development (5.1%) was performed with the funds from the National Investment Plan. It was then the support to agricultural production and market of agricultural and food products (38.1%) were reduced, while simultaneously the share of public participation and professional services costs (36.1%) was increased.

The funds of the agrarian budget in this period were insufficient to meet the current and development needs of agricultural production, which directly affects the structural adjustment to requirements of the European Union.⁷ Government funds are inadequate related to the importance of agriculture in the structure of domestic production, because in this period the share of agriculture in GDP achieved an average of about 19%, and with the related industries about 40%. At the same time the share of agriculture in total exports is about 25%, while the state budget funds for support of agriculture amount 5%, which is significantly less comparing to neighboring countries (10% to 14%).⁸ Subsidy funds were reduced in this period, because a part of the funds was invested in the form of loans, which according to the expert opinions was inconsistent with the basic function of the agrarian budget related to provision of the non-refundable incentives. Funds from the agrarian budget do not correspond to the importance of agricultural production, including the AP Vojvodina, where they ranged from 2.4% to 3.9% in the period 2004-2006. The analyzed period is characterized by not solving the problem of financing of the agricultural production, and inadequate financial support of the government to this important economic activity. The Government of the Republic of Serbia has in 2009, based on the Budget Law, adopted the Regulation on the use of funds to support rural development through support of the agricultural investments. Incentives are related to the construction of facilities, cold storages, silos and the procurement of certain equipment in agriculture. An agricultural cooperatives and private individuals, i.e. holders of the agricultural estates, have the right to use these incentives, with certain exceptions. The right to use non-refundable incentives is conditioned with providing the amount of own funds for the realization of investments. The amounts of funds are determined depending on the character of certain areas. In the Article VII of the Regulation the maximum amounts and percentages of incentives in relation to the total value of investments were precisely determined depending on their purpose.

7 Simić, N. (2006): *Poreski sistem kao faktor ruralnog razvoja*, Ekonomika poljoprivrede, Beograd, br. 2/2006, str.253-267.

8 Pejanović, R. (2009): *Razvojni problemi poljoprivrede Republike Srbije*, Agroekonomika, Beograd, br. 41-42/2009.

The measures of institutional support

Regulation on the abatement of the agricultural production was adopted in March 2012, defining the conditions for the use of incentives for investment in production and placement of certain agricultural products. Farmers are entitled to a refund of insurance in the amount of 40% of the premiums. Beneficiaries and other conditions are precisely determined in Regulation. Regulation on the establishment of credit support for investment in agricultural machinery and equipment through the subsidization of interest rates was adopted by the Government of the Republic of Serbia in 2012. Credit support is achieved through subsidizing the part of the interest that banks charges to borrowers, in order to encourage agricultural production. Entrepreneurs, legal entities and individuals are entitled to use funds, i.e. to credit support for investment in specified agricultural machinery. Introducing a regulated system of subsidies for the production of beef and pork is planned, which should enable an increase in livestock fattening and meat production and a reduction of the underground economy.

In the Law on Agriculture and Rural Development, the direct structural and market incentives are precisely determined, depending on the difficult working conditions in agriculture. Direct incentives are related to premiums, incentives for production, allowances and support for non-commercial farms. Forms of market incentives are export incentives, storage costs and credit support. Structural incentives include measures of rural development, quality improvement and protection of agricultural land and the measures of institutional support, where those of financial nature have the predominant importance.

The global economic and financial crisis has, according to assessment of international institutions, affected the continuation of the trend of increased consumption of agricultural products. Developing countries are unable to produce the necessary quantities of food and hence are forced to import. Thus, in the period 2000-2007 a pressure on the prices of agricultural products has increased. Foreign investments in agriculture have amounted to USD 32 billion, which represents only 0.2% of total foreign direct investment. The trend of reduction of foreign direct investments in agriculture of the developing countries is continued, which is conditioned by administrative barriers, the political sensitivity of the agricultural sector and the limitations of the system of ownership over the agricultural land. Impacts of international corporations on agriculture extend beyond the direct foreign investments, since they are oriented to variety of short-term and long-term arrangements with local farmers rather than to ownership investments. There are new investors in the world emerging in the sector of agriculture, such as civil, and venture capital funds. There is also a growth of investments between developing countries, while international companies focused their investments in production of meat, flowers, fruits and vegetables in developed countries. Their investments in developing countries are directed to specific export products, mainly oilseeds, soybeans, fruits and sugar cane. Trend of growth of certain products imports is continued in the underdeveloped countries, which is conditioned by rising consumption of food products. During the food crisis, barriers to foreign investments in agriculture in the developing countries must be eliminated.

The stabilization and development objectives in agriculture

Modern agricultural policy implies an active agrarian budget directed towards the development of SMEs and entrepreneurship. In determining the basis of current agrarian budget, and ensuring stable and affordable source of funding it is necessary to take into account the impacts of globalization, the need for ensuring food assurance and rural entrepreneurship and the development of small and medium enterprises, social security, the humanization of work, quality of food and care about the environment, sustainable development and others. This requires strengthening of the institutions of agrarian loans in a specific economic environment in the EU accession process, which includes the legal harmonization in the field of agriculture.⁹ It should be noted that in this process there are upcoming significant changes and challenges relating to quality standards, rural development, new opportunities for export of competitive products, and increased import competition in the domestic market of agricultural and food products, due to reduction of customs protection. This requires increased investment in agriculture in accordance with European standards and the importance of agriculture for the economy of the Republic of Serbia. In this process it is very important to get familiar with a way of subsidizing agriculture in the European Union. Significant investments in the agricultural sector are necessary in order to take advantage of the huge potential in the agricultural and food sector. It is illusive that the development objectives in agricultural production can be achieved without a developed financial market. It is undisputed that a large number of natural, demographic and economic factors affect the agricultural development in various stages of development of the Republic of Serbia, within which those factors of financial nature are very important. The fact that the stabilization and development objectives in agriculture need to be achieved in the terms of the financial crisis, i.e. the decrease in foreign direct investment, purchasing power and income of farmers, represents a difficulty. In addition, the industrial sector is characterized by continuous increase in prices of agricultural inputs and low purchase prices of certain agricultural products, while in the trade sector there are relatively high margins on agricultural and food products, the long contract terms and violations of payment schedules of the agricultural products. The situation is aggravated by the condition of the banking sector, in which there are high interest rates and prices of ancillary services. Negative tendencies are being deepened due to the global economic crisis and decrease of the credit potential for agricultural production. In drafting of the primary objectives of the agrarian policy a successful examples from the region should be taken into account, particularly from Bulgaria, Hungary, Slovakia, Kazakhstan and Ukraine, referring to legislation, inspection services, and export credit policies, public warehouses, commodity reserves and electronic reserves.

Changes in rural development and agricultural production require reform of fiscal and tax policy. Changes related to various fiscal forms cause different effects on agricultural development. Solving of the complex development problems in agriculture is not possible without considering tax incentives and exemptions. Requirements refer to the increase and the allocation of funds intended for agriculture in Serbia. Loan funds represent the additional

9 Vlahović, B., Tomić, D., Gulan, B. (2006): *Priprema agrokompleksa Srbije za evropske integracije*, Ekonomika poljoprivrede, Beograd, br. 2/2006, str. 122-125.

funds to those contained in the agrarian budget. Grants are directed towards the stabilization of the agricultural products market, encouraging of the development and structural changes. The importance of the investment loans is also emphasized in the agrarian policy, as well as those loans aimed at ensuring an effective system of stocks and seasonal agricultural products reserves, the smooth running of production and the necessary working capital. The new tax exemptions and incentives to local authorities are directed towards stimulating agricultural production, increasing of the investments, enlargement of the estate and others. In technical terms the proper establishing of the tax base and precise definition of tax exemptions is required.

In drafting of the goals and measures of the agricultural policy contained in the National agriculture program of Serbia, in the following years, it is insisted on considering of specificities of the environment characterized by rapid growth of the demand for agricultural products, particularly in the developing countries, the expected increase in volume of agricultural production in the world, by declining growth rates. Enlargement of the European Union also affects the changes in the market of agricultural products. New strategies must be based on the principles of the EU, WTO and CEFTA.¹⁰ There is an orientation towards market liberalization and free international trade with the support to agricultural development, in accordance with international standards, particularly in the financial sphere. Only in this way it is possible to utilize the great potential of Serbia in the agricultural sector. This includes changes in ownership structure and the enlargement of estates, institutional support, measures for increasing of the exports and competitiveness of agricultural production and development of the loans market.

Favorable trend is included in the tendency of growth of the food prices in the world. Priority objectives in the future are related to the improvement of the work of the institutions, increased investment, joint programs, commercial-crediting and financial activities, improving of the competition, quality and other agricultural inputs. It is necessary to develop credit lines and to establish the Funds for Agricultural Development at various levels and develop a system of subsidies and procurement of agricultural inputs. It is desirable to develop a system of subsidizing insurance premiums and compensation for damage from natural disasters. There is also an orientation towards building of regional and local institutions to support rural development, particularly in the areas of investment activity.

It is especially important to prepare agriculture for accession to the European Union so that Serbia would be able to withstand competition in the free European market. In doing so the basic principles of the WTO also should be taken into account, which are related to the reduction of external protection, the elimination of export subsidies and certain non-customs barriers etc.

The necessity of increasing the agrarian budget is based on the needs for increasing competitiveness in the EU accession process and taking into account the attitude that

10 Katić, B., Popović, V., Milanović, M. (2008): *Uticaj sporazuma o stabilizaciji i pridruživanju na poljoprivredu Republika Srbije - globalni pristup*, Ekonomika poljoprivrede, Beograd, br. 4/2008, str. 340-342.

agriculture is viewed as a comprehensive rural development. In the short term it is planned that the share of the agrarian budget in total budget amounts to about 5%. The structure of the budget should be aimed at increasing of the investments, funds for rural development, reducing of the administration costs, export subsidies and the share of the financial support in earned realized income. To this end, it is needed a long term planning of the measures and the necessary budgetary resources, with respect to basic principles of reform of the policy of agricultural production and trade in the agricultural products market in the European Union, which means the separation of subsidies from production, the new social assistance system, the introduction of quality standards and environmental protection. It is also understood to achieve a high degree of financial discipline in the implementation of agricultural policy. The goal is the gradual reduction of direct expenditures for the agriculture and precise statement of the requirements for EU aid in achieving the objectives of rural development.

New measures should include investments in agricultural estates, improvement of production and marketing of agricultural products, professional training and support to young farmers, afforestation and environment. New initiatives are instruments of support for EU rural policy. Thus, the SAPARD program was created to support the growth of agricultural production and support rural development policy in the period of EU accession. New programs of assistance to support rural development are contained in the new instruments and programs of the pre-accession assistance (IPA).

In the accession process it is necessary to stop the long-term negative trends in the national economy and to change the role of agriculture as a social stabilizer in times of global economic and financial crisis, especially as it affected not only the inflow of direct foreign investments, but also their outflow from Serbia and the region. Agriculture, according to available resources, should become an export business, i.e. the strategic orientation in the policy of the agricultural production development. Analyses indicate inefficient use of available resources, and lack of stimulating nature of economic, particularly financial measures in agrarian policy of the Republic of Serbia. The new agrarian policy requires taking coordinated actions and measures related also to the establishment of agrarian development banks and other financial activities in the terms of global economic crisis.

Conclusion

The research results confirm that in order to take advantage of large agrarian potentials of Serbia in the terms of financial crisis and the lack of foreign direct investment and loans, there is a need for more fiscal support for agricultural production. This determination is fully consistent with the economic importance of this priority sector, which together with food and related industries creates about 20% of the GDP. The funds from the agrarian budget do not correspond to the importance of agriculture (funds for subsidies in agriculture in the budget of Serbia for 2012 amount to only RSD 19.9 billion, representing approximately 2.45% of total budget) and its export capabilities. At the same time this poses a danger to make it uncompetitive in the international market, especially after the accession to the European Union when it is necessary to reduce customs restrictions. If in the next short period the funds from the agrarian budget do not increase significantly, in accordance with policies in

the region and EU countries, it may happen that a great opportunity for development of the Republic of Serbia, in terms of production and export, remains unused with unpredictable macro-economic, political and social consequences. So it should be strived towards greater government assistance in the financial sphere, and provide measures to support agriculture through monetary and fiscal measures and instruments. At the same time, it is necessary in short term to significantly increase funds for agriculture to the level of about 5% of budget funds. By efficient implementation of fiscal measures in coordination with monetary support, the adverse position of the agriculture, i.e. its share in exports and realized GDP can be improved in the short term. There are real opportunities for substantial increase in gross and net value of agricultural production, which now amounts to five, i.e. four billion dollars, and exports, which now does not match the great potential of agriculture and is only about two billion dollars. It is unacceptable that the export of agricultural products per hectare of arable land, or per capita is about three times lower than in Central and Eastern Europe. Therefore, the government must take urgent measures also in the fiscal policy and increase the incentives from the budget of Serbia, which now amount to USD 29 per farmer, while in the European Union that value is USD 130.

The preparation of the Serbian agriculture for free competition in the European market is becoming an imperative for current economic situation, especially in the terms of existing world financial crisis and the demands of the EU accession process. That, in accordance with international standards, requires changes in the way of providing of government support to agriculture development, i.e. the introduction of a series of stimulus tax incentives and exemptions, in accordance with the European Union's agricultural policy.

Active agrarian budget should be focused towards the development of SMEs and entrepreneurship. Fiscal reforms and substantial fiscal support to agriculture, as the development opportunity of the Republic of Serbia, should help agriculture in order to use its development, especially export potentials. Budgetary policy has to provide optimum support to specific agricultural production and rural development.

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NOVA FISKALNA ULOGA DRŽAVE U TRANZICIJI POLJOPRIVREDE SRBIJE

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Rezime

U procesu pridruživanja neophodno je iskoristiti ogromne potencijale u poljoprivrednom i prehrambenom sektoru u Republici Srbiji. U uslovima svetske ekonomske krize, nedostatka stranih direktnih investicija, nepovoljnog stanja u bankarskom sektoru i neracionalnog korišćenja raspoloživih resursa, potrebno je pripremiti poljoprivredu da bi bila u stanju da izdrži slobodnu konkurenciju na evropskom tržištu. U tom smislu treba pružiti veću podršku poljoprivrednom razvoju, saglasno međunarodnim standardima, posebno u načinu državne podrške poljoprivrednom razvoju u fiskalnoj sferi, odnosno uvođenju niza stimulativnih finansijskih mera u agrarnoj politici Republike Srbije.

Ključne reči: *poljoprivredna proizvodnja, Republika Srbija, fiskalna i agrarna politika, agrarni budžet, subvencije, ruralni razvoj i pridruživanje Evropskoj uniji.*

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