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Transition to the agricultural land market with the minimal risks

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1. Introduction

According to the coalition agreement, which was signed when the parliamentary majority was formed, the transition to agricultural land market is not planned in the near future (Verkhovna Rada (2014)). However, the transition to market economy makes it possible to transfer the land as means of production to more efficient owners and therefore contributes to social welfare (Just R.E., Hueth D.L., Schmitz A. (2014)). The absence of a land market has a negative impact on the development of agricultural production, hinders to its capitalization and creation of the infrastructure of agricultural production increases, increases the business risks.

2. Data and Methods

We will explore the features of the land market in the European union countries.

3. Results

Subsidy factor has a decisive influence on land price according to the latest date (Farmland investment). Subsidies and 1 ha land price for some countries (Table 1) illustrate this fact. Discount rates for these countries is also presented.

Table 1. The subsidies, hectare price and discount rates in EU countries (EUR)

Netherlands		Poland		Germany		Romania		Bulgaria	
Subsidy (rate)	price	Subsidy (rate)	price	Subsidy (rate)	price	Subsidy (rate)	price	Subsidy (rate)	price
450 (0,75%)	40000-80000	210 (3,2%)	8000-13000	320 (0,64%)	20000-80000	200 (4%)	2900-7000	100 (8%)	1200-1300

Source: Farmland investment.

There is a connection between the amount of subsidy and one hectare price. In developed countries there is a tendency of the decrease of the ratio of rent to land value, which is caused by rapid increase in the land price (Janssen I., Dillivan K., McMurtry B. (2014); Swinnen J., Ciaian P., Kanks A. (2008)). For Ukraine transition to the land market is connected with risks of excessive supply because of the big land fond. Among three categories of Ukraine agrarian entities: households, businesses and state-owned enterprises the least effective are state companies because they are unprofitable according to the utility theory (their management costs are more useful than income), and significant budget sums allocated annually for their support.

Therefore, as one of the transition options we can suggest the establishment of land market with limited supply through agricultural state enterprises, with the volume of deals which does not exceed 1 million hectares (Table 2).

Table 2. The available areas and their allocation

Agricultural assignment	Area (mil.ha)	Part (%)	Users number (mil.)	Profitability(%)
Land shiers	27,7	100	6,9	
Rent	17,4	62,8	4,5	22-35
Used householders	4,4	15,9	1,2	10-30
Not identified	4,3	15,5	1,2	
state-owned enterprises	1,1	5,8	0,024	-5-7

Source: State Statistic Service of Ukraine (2012).

Such an amount does not exceed 4% of total agricultural land which corresponds to the annual supply of land in the EU. This means that with some confidence (based on the experience of neighboring countries) we can determine the lower limit of the revenue from the sale of 1 million hectares of state enterprises, which is approximately equal to \$ 500 million.

To assess the potential financial capacity of land market participants we analyze the profitability indicators of 9120 agricultural enterprises with possess land (form SG-50).

Approximately 30% of enterprises are low-profitable or unprofitable (return is less than 10%). The share of highly profitable enterprises (return more than 50%) is more than 20% (Fig.1). These enterprises are potential participants of land market.

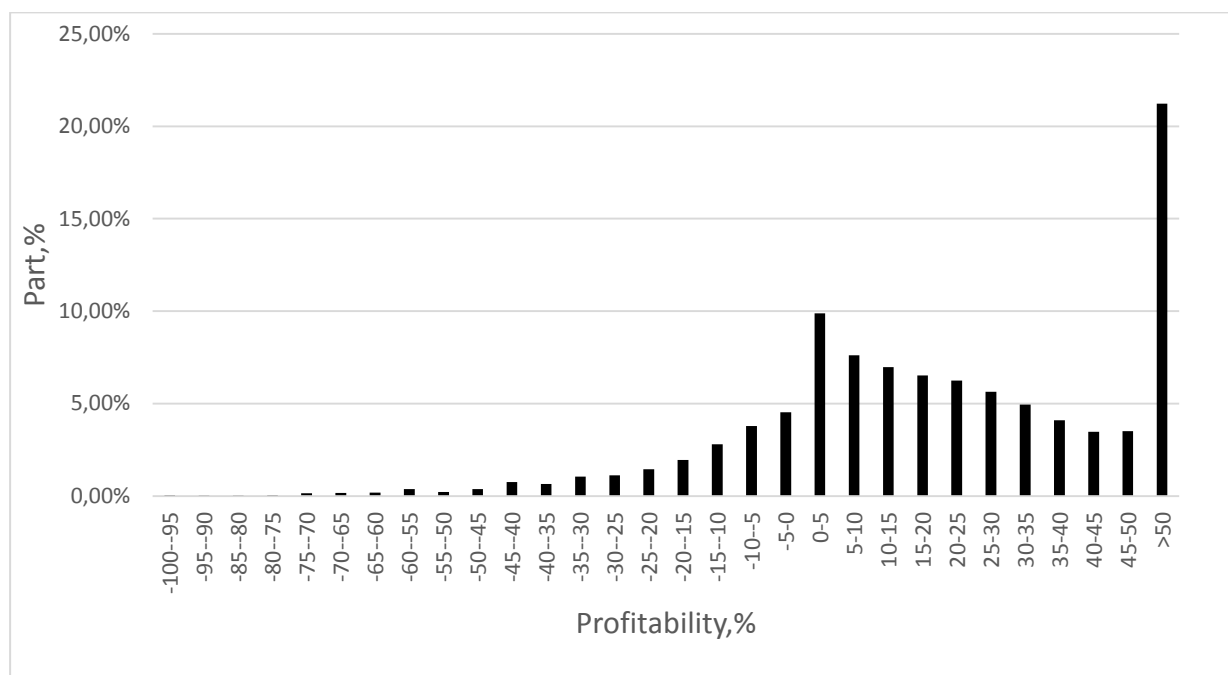


Figure 1. Agrarian enterprises profitability 2013 distribution

Source: Own compilation and calculations.

Gradual transition to agricultural land market will not bear significant risks for food security, but has rather limited social risk regarding employment of 24 thousands of state agricultural employees (Table 2). The possible solution can be allocation of land with an average size.

Limited supply in the land market will not have a significant influence on the rental market. There can be a slight decrease in income of households and increase in the income of agricultural enterprises due to reduced rent (in the amount that does not exceed 4%).

The growth of the income of the state on the basis of the money got from the selling the land of unprofitable agricultural enterprises can be estimated from \$ 500mln to \$ 1.5 billion.

4. Conclusions

We propose the first step towards transition to agricultural land market, in the which the supply is based on the land of agricultural state enterprises. In this case, will be created a land market with a limited land supply for which the equilibrium price will be higher then in the case of unlimited supply.

Limited supply in the land market will have no influence on the rental market. It is possible that a slight decrease in household incomes and increase in the income of agricultural enterprises because of the reduction of the rent (in the amount which does not exceed 4%). This decrease will not be felt on the background of the general trend of rent and land value growth, which is possible only with increase of the level of efficiency of agricultural production.

Further steps towards functioning of agricultural land market (the volume of annual supply) can only be done on the basis of careful analysis of the economic and financial implications of the first step (limited supply).

Efficiency of the most efficient producers is the main factor that determines the price level under the conditions of limited supply and macroeconomic instability.

The increase state revenue through funds received from the sale of agricultural land of unprofitable state enterprises can be estimated from \$ 500mln to \$ 1.5 billion.

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