

# BRANCH-WISE ECONOMY

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## Improvement of state regulation of the agrarian sector of the sub-arctic and arctic areas under the WTO membership



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**Abstract.** The article substantiates the necessity to change the role of the state in technological and socio-economic development of the agricultural sector. The author considers the forms and methods of state regulation and analyses the current budget support provided to agriculture; he highlights its drawbacks with regard to sub-arctic and arctic territories of the Republic of Komi. The article shows the influence of state support on the farmers' level of income and identifies modernization risks and threats under Russia's WTO membership. The author proposes measures to improve state support of the agrarian sector and change the adverse conditions of its functioning. He substantiates the approach that helps improve the state regulation of the agrarian sector in the framework of regional and municipal programs for rural development.

**Key words:** agriculture, state regulation, financial support, WTO, Arctic sub-region, Republic of Komi.

### Introduction

In the course of market reforms, the North experienced the dramatic reduction in government support and investment, the destruction of material and technological base of agriculture, the outflow of qualified personnel from the industry and the decline in production [3, 10].

The current state of the agricultural sector of the northern and arctic areas is characterized as unstable; it can become extremely negative and lead to the elimination of agricultural production, primarily, in peripheral (remote) areas and to the reduction of inhabited rural areas. The crisis can be overcome and the transition of

agriculture to the dynamic development can be achieved, if a multi-purpose agricultural policy is pursued taking into account the specifics of the North; the policy should focus on the technical and technological modernization of agricultural production, on the formation of multistructural and multifunctional agriculture in rural areas, on the strengthening of state support of agricultural producers. The implementation of technological and socio-economic development of the rural economy of the North and the Arctic will require substantial financial resources, including public investment.

The goal and objective of this work is to analyze the financial support, to identify its shortcomings and to substantiate the measures undertaken to improve state regulation of agriculture in the Arctic sub-region on the example of the Komi Republic.

#### **Strengthening the role of the state in the development of modernization processes in the agrarian sector**

The role of the state as the organizer and coordinator of modernization is becoming more important not only due to its increasing significance in the economy and society, but also due to the specifics of agriculture and market relations in the industry. The agricultural sector in general and, especially, in the northern and arctic areas does not fit into the modern market economy model and can be developed with government support. The objective necessity of state regulation of agriculture consists in the following.

1. Demand for food stock is not very flexible. Demand is determined not only by economic factors such as consumers' incomes and food prices, but also by

physiological needs, which have strict limits. When retail prices grow, people reduce their demand for high quality food.

2. Agriculture is a relatively conservative industry and can not immediately change its structure and production technology. The duration of the production cycle in the majority of agricultural industries means that, regardless of the market situation, the scope of supply cannot be reduced or increased within a short period of time.

3. The food market has two non-flexible components – food demand and supply. During the periods of rapid food prices fluctuations the government should take measures to regulate the agrifood market.

Currently, the competitiveness of agriculture in the USA and Western European countries is maintained with the help of government intervention, i.e. by the methods opposed to the approach presented in the theories on perfect and imperfect competition. The models of the market of perfect and imperfect competition are a theoretical abstraction that has nothing to do with actual practice [12, p. 293].

4. The need for the state regulation of agriculture is caused by the fact that a non-exclusive agricultural market is confronted by the oligopolistic structures of the first and third spheres of the agricultural complex that establish the so-called administered prices.

5. Agriculture is the sector of production and, at the same time, the sphere of human activity. The elimination of agricultural production means the change of place of residence and lifestyle for the people. The limited competitiveness of rural residents in the labor market urges the farmers and the public to defend the programs for state support of agriculture.

The government intervention in Russia as a whole and in the North and the Arctic in particular is necessary also due to the following reasons:

- extremely low level of productivity and remuneration in the sector;
- disparity in prices for industrial and agricultural products;
- significant expenditures on land management and reclamation given a relatively low return;
- incompleteness of the processes of intensification and industrialization of agricultural production; intensification and the transition to industrial production methods are connected with the high demand for continuous investment at a relatively low capital productivity ratio;
- poor development of rural industrial, social and financial infrastructure.

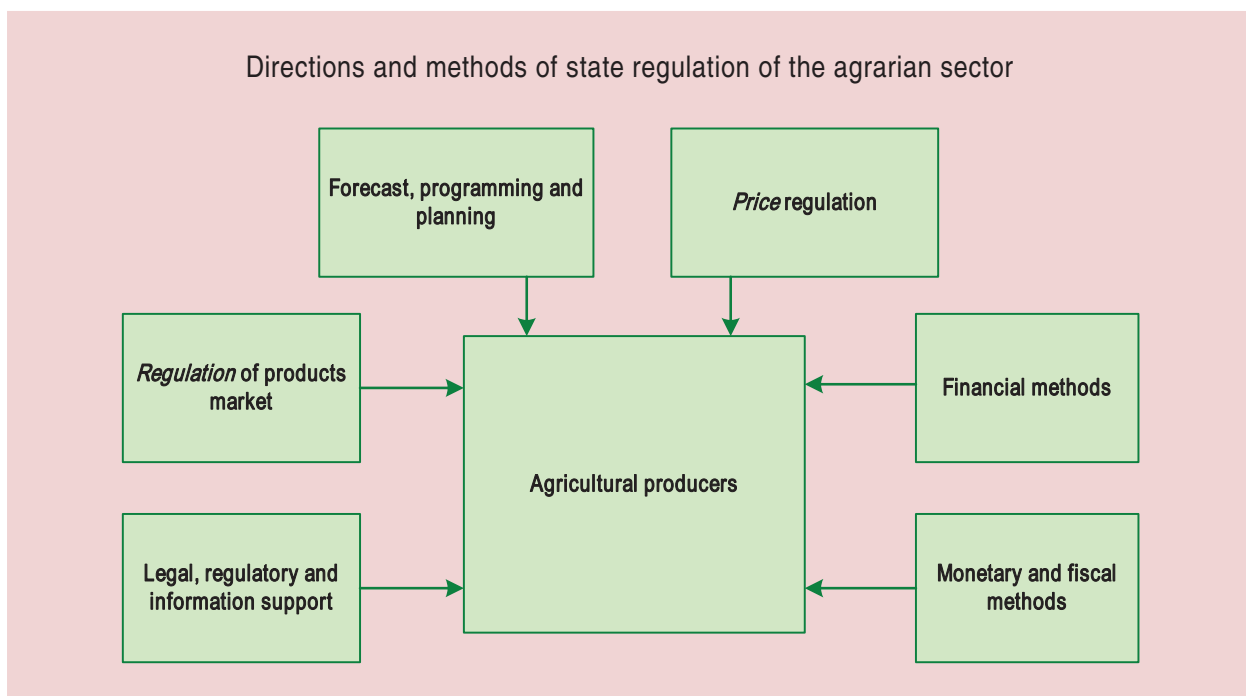
Under the extreme conditions in the North and the Arctic, in contrast to the southern and central regions of the country,

private capital is not interested in investing in the preservation and development of agriculture. Here the role of the state is especially important in financing the agricultural sector.

Disregard for the special nature of agriculture as a specific sector of the national economy and insufficient financial support to the agricultural sector are the main causes of the crisis in the industry. The solution of the problem of the agricultural sector modernization will require a manifold increase in the volume of subsidies.

Regulation has a multidimensional character from the point of view of its implementation method and the objects, on which it is focused. Directions and methods of government's influence on the reproductive process in agriculture are shown in the *figure*.

The agrarian reform carried out in Russia in the 1990s was characterized by the invalidity of a number of measures, by



contradictions and inconsistencies in the transformations implemented. Socio-economic orientation of agrarian transformations was replaced by the self-contained task of hasty transition to the market economy.

Regional characteristics were not taken into account to the extent necessary; in particular, the fact that agriculture in the North is developing under extreme conditions, with limited material and technological base and sphere of agro-service, poor housing conditions and underdeveloped social infrastructure of the village. Historically, the region developed a community-based land use system, and, therefore, the psychological determination of people to work and live as a team is expressed to a greater extent compared with Russia's southern regions. One of the reasons for the crisis in agriculture was the implementation of the wrong measures aimed at the immediate and complete liberalization of economic relations and the abandonment of state support of the agrarian sector.

Since 2006 the Russian Federation has been implementing the national project "Development of the agro-industrial complex" transformed into "The state program for development of agriculture and regulation of markets of agricultural products, raw materials and food for 2008–2012 and 2013–2020". The project focuses on the provision of state support to the development of animal husbandry and small farms.

#### **Analysis of existing financial support to agriculture**

The implementation of the priority national project "Development of the agro-industrial complex" contributed to the

financial support of agricultural producers. The volume of subsidies provided to the agriculture of the Komi Republic for 2006–2012 has increased by more than 1.8 times. The state support to the agricultural sector is mainly provided from the regional budget. Now 84% of subsidies to the sector is allocated from the budget of the Republic, 14% – from the federal budget and 2% – from the local budget. According to the forecast estimate provided in "The state program for the development of the agro-food sector in the Republic up to 2020", the share of subsidies from the budget of the Republic will increase to 91% and the share of subsidies from the federal and local budgets will decrease, respectively, to 8 and 1%.

The subsidies allowed the majority of agricultural producers in the arctic and subarctic areas to avoid losses. Without obtaining financial support, agricultural organizations, except those specializing in reindeer breeding, fish harvesting and processing, suffer huge losses. However, even with the subsidies, the level of profitability in the majority of agricultural enterprises will remain very low, and some of them are unprofitable (*tab. 1*).

The analysis of the existing financial support proves that its significant proportion falls on large agricultural enterprises with more resources, and on suburban areas. At that, the support is not always proportional to the volumes of produced agricultural products. In 2012 the farmers at the peripheral subarctic areas (Ust-Tsilemsky and Izhemsky) received only 4.5% of the total amount of subsidies to agriculture of the Komi Republic, while their share in the volume of gross agricultural production was 7.1%. Only 1.4% of the subsidies out

Table 1. Profit (loss -) and profitability of agricultural enterprises in the arctic and subarctic areas of the Komi Republic in 2012

Municipal entity, organization	Profit (loss -) from sales, thousand rub.	Profit (loss -) before tax, thousand rub.	Net profit (loss -), thousand rub.	Profitability (unprofitability -), %	
				Excluding subsidies	Including subsidies
Urban district Vorkuta	107	22141	21954	0.2	34.2
Agricultural Production Cooperative "Olenevod"	785	22124	21937	1.3	36.9
LLC "Sovkhoz Gorodskoy"	-678	17	17	-15.3	0.4
Urban district Inta	-43892	-802	-1548	-16.5	-0.6
LLC Agroindustrial Farm "Inta Pripolyarnaya"	-44121	-5411	-5876	-18.5	-2.5
OJSC "Petrun'skoe"	-1300	3103	3103	6.7	15.9
OJSC "Abez"	-1071	1446	1225	-15.5	17.7
Urban district Usinsk	-44396	-2481	-2753	-27.3	-1.7
LLC "Kolva"	-8330	-2742	-2764	-47.9	-15.9
LLC "Severnyy"	-36066	261	11	-24.8	0.0
Municipal district Pechora	-4221	7979	7652	-14.1	25.5
LLC "AgroVid"	-3063	6965	6638	-10.2	22.2
LLC "Akvakompleks"	-1158	1014	1014	-95.3	83.5
Municipal district Ust-Tsilemsky	-15309	4077	3361	-27.6	6.0
APC "Zarya-1"	-2274	3283	3058	-14.8	19.9
LLC "Veles-Agro"	-1084	274	274	-58.4	14.8
LLC "Rochevo"	-2795	880	788	-33.7	9.5
APC "Mayak"	-1611	585	491	-39.7	12.1
LLC "Filippovo"	-1182	298	250	-31.9	6.7
LLC "Trusovo"	-2361	800	790	-26.5	8.9
LLC "Zvezda"	-4008	-1940	-2034	-51.2	-26.0
Municipal district Izhemsky	-8644	4125	4118	-28.4	13.5
APC "Agro-Tsentr"	-4111	421	421	-29.1	3.0
LLC "Zarech'e"	-1566	4222	4222	-19.0	51.2
APC "Borovaya"	-2967	-518	-525	-36.9	-6.5

Source: annual statements.

of the total volume of financial support of this sphere is directed to the infrastructural and technological modernization of the producers in these areas. At the same time, fixed capital assets in animal husbandry in the arctic and subarctic areas are worn by 70–80%.

The data on the volume and share of subsidies to agricultural producers in the

arctic and subarctic regions of the Republic are shown in *table 2*.

Thus, the existing volume of state support to the agrarian sector in the subarctic region of the Komi Republic is insufficient not only for innovation development of agriculture, but even for curbing the decline in production. The creation of conditions for the dynamic

Table 2. Subsidies to agricultural producers in the Komi Republic in 2012, thousand rubles

Directions of state support	Komi Republic	Subarctic region	Share of the subarctic region in the total amount of support provided to agriculture of the Republic, %
Subsidies for livestock products	305783	71328	23.3
Out of them: for cattle meat	27674	9264	33.5
milk	214587	43223	19.7
Subsidies for increasing the deer population	25507	25507	100
Subsidies for modernization of technology and equipment	175146	27807	15.9
Subsidies for fodder	91499	16363	17.9
Other subsidies and subventions	238063	58729	24.7
Total	835998	199734	23.9
Source: annual statements.			

development of agriculture requires strengthening of its state support.

The accession of the Russian Federation to the WTO has introduced significant adjustments in the system of state regulation. Russia has assumed a number of obligations on the state support to agriculture, export and import duties, tariff quotas, and export subsidies.

As for the customs-tariff regulation, the risks are mainly associated with the reduction of tariffs on agricultural products and foodstuffs from 15.6% at present to 11.3% at the end of the transition period (2018). According to experts, serious adverse effects from tariff reductions are expected in the pork and beef market. Our country is to reduce customs duties on live pigs from 40 to 5%, and the duties on pork imports within the quota will fall from the current 15% to zero. A ban on further reduction of quotas has been imposed.

A serious threat to agriculture is the growth of prices of energy, facilities, equipment, and other resources, since it

reduces agricultural producers' incomes. The World Trade Organization demands that Russia bring its internal gas, oil and electricity prices to the world level; that is, raise them by the 1.3–1.5 times, so that the Russian industry did not have economic advantages in the production of materials, equipment and other resources in comparison with the Western industry. Besides, Russia is to reduce customs duties on the import of agricultural machinery by 2–3 times in order to facilitate the import of foreign cars. According to the calculations of Rostselmash (Russian agricultural equipment company), the import of agricultural machinery will lead to the rise in its prices on average by 20%, and the increase in the costs will be over 31 billion rubles per year. The limitation of fuel prices subsidizing for the village will cause their growth by 25–30% and will increase the costs of rural producers by 39.8 billion rubles per year [1, p. 51]. This limits their opportunities to carry out modernization and innovation

development. Prior to its accession to the WTO, the state annually issued direct subsidies in order to compensate partially for the losses from price disparity between agricultural and industrial products.

State support plays an important role in the development of the agricultural sector. Therefore, the amount of state support at the time of Russia's accession to the WTO is the main subject of disputes in the agreements on agriculture. Under the WTO Russia and its regions must adhere to the restrictions of budget support to the sector and change the directions of its subsidizing. The level of support permitted under the WTO is divided into three types – three “baskets”, which are divided into “green”, “yellow” (“amber”) and “blue”, depending on the degree of distorting influence on trade.

The “green basket” includes support measures that do not have negative impact on trade, the “yellow basket” comprises measures that distort the market. The level of state support to “yellow basket” for our country for 2013 is defined at 9 billion U.S. dollars with further reduction by equal shares to 4.4 billion U.S. dollars by 2018. The “blue basket” includes budgetary payments aimed to limit agricultural production.

Financial support to the producers of agricultural products and foodstuffs in the Komi Republic is currently provided in the following directions:

- provision of subsidies for technological and equipment modernization of agricultural production;
- compensation for a part of expenses for cattle management;
- provision of support to livestock breeding;

- reimbursement of a part of expenses for purchase and manufacture of combined fodder;

- reimbursement of costs for the increase in reindeer population, for the implementation of fire safety measures at reindeer pastures, for reindeer veterinary services;

- provision of support to elite seed farming;

- subsidizing measures to improve soil fertility;

- free support to crop sector;

- support to small forms of business.

- subsidizing the development of aquaculture and fishery.

#### **Improvement of state support to the agricultural sector**

Private entrepreneurs in the condition of the North, due to the low profitability of agriculture and considerable payback period, are not interested in investing in its development. Here the bulk of financing in technological and equipment modernization of agricultural production falls on the state. The increase in profitability and investment opportunities for the agricultural sector requires a significant increase in direct state support. The subsidies provided to agricultural producers allow them to earn income in addition to profit from sales of their products, without affecting the growth of food prices. If there is no support to producers' incomes through subsidizing the prices of manufactured products, the efficiency of investment will be very low; they may not even pay off.

The economic assessment of innovation-investment projects for the construction of dairy farms for 100 and 200 cows in the peripheral Udorsky District with the use of the latest technology, with high productivity

of the cows (5500 kg) and adherence to the principles of production of organic products has shown the following results. Under the existing sufficient state support to innovation-investment activity and the profit of the agricultural producers, these projects will pay off only in 12.5 and 11.3 years if the loan is granted for the term of 8 years. Only when the volume of state support to provide the optimum level of profitability (40–50%) is reached, the payback period of the projects will be below the terms of the loan granted [4].

To speed up the modernization of agricultural production, it is necessary to increase direct state support by 3–4 times, and for individual agricultural enterprises – by 4.7–5.1 times [9, p. 215]. Public investment is also necessary to achieve this goal.

For the speedy transfer of agricultural economy to the new technological basis it is suggested to subsidize it not only from the regional budget, but also from the federal budget. It is advisable to use the federal budget to carry out state support to increase the cattle and deer population, to boost the production of beef, venison and milk; to compensate for part of the cost of modern technology and equipment, mineral fertilizers, fuel, spare parts, combined fodder, and also tariffs in the amount of 50% at the transportation of material and technical resources by railway and water; to subsidize interest rates on loans; to provide subsidies for poverty alleviation in the rural population. At the same time, it will require the elaboration and adoption of federal target programs for the development of reindeer herding and elimination of rural poverty.

At the regional level is necessary to maintain financial support to the

construction and reconstruction of livestock facilities, purchase of new machinery and equipment, production of livestock and reindeer products, subsidizing interest rates on loans. It is proposed to issue targeted subsidies for starting a business in order to develop entrepreneurial activity in agriculture, fishery and processing of their products; also in the forest sector and tourism.

It is necessary to preserve the subsidizing of interest rates on loans for companies in the agricultural and food sector, to free the agricultural producers from paying property tax and transport tax. Regional authorities can adopt the necessary legislation that provides for exemption of investors from property taxation and transport taxation that goes to the regional budgets, and for the provision of guarantees when applying for a bank loan.

In order to attract qualified specialists into agriculture and fishery the state should create necessary conditions of life for them. For example, it is necessary to establish lump sum subsidies in the amount of one million rubles for university graduates who are employed in the agricultural sector and in the amount of 600 thousand rubles – for technical schools graduates, who are also employed in agriculture. It is necessary to establish the wages for young professionals that would be higher than the regional average, and to provide cheap mortgage (2–3%). In turn, young specialists are to work in rural areas for at least five years.

It is obvious that under the WTO the agriculture of the northern and arctic territories, which has not overcome the crisis of 1990–2000, will face new challenges in the technological and socio-economic development of the sector. The



risks and threats include the reduction of investment attractiveness and profitability of enterprises and households, which hampers agricultural sector modernization; the failure to implement the indicators set out in the Food Security Doctrine of the Russian Federation; the bankruptcy of agricultural enterprises and peasant-farm households due to low competitiveness; the reduction of the number of jobs; the reduction of tax revenues from the agricultural and food sector; the reduction of incomes and deterioration of the standard of living of farmers. In this regard, special importance is attached to the development of measures to prevent the aggravation of the socio-economic situation in agriculture and fishery. It is necessary to remove restrictions on the “yellow basket” for the northern and arctic areas that have extreme conditions for agriculture. The removal of restrictions on the provision of agricultural support to the zone of the North will increase the profitability of agricultural production and wages of its employees, ensure their employment, provide more investment opportunities for the modernization of cattle and reindeer breeding.

One of the most important decisions is to amend the Federal Law 2006 “On the development of agriculture” that provides for the identification of RF subjects with unfavorable conditions for farming and makes it possible to remove restrictions on the state support to agricultural enterprises in these regions allowed by the “yellow basket”. In order to abandon the restrictions, the Ministry of Agriculture of Russia has identified 63 subjects with adverse conditions for agriculture development.

Under the conditions of Russia’s membership in the WTO it is also useful to

exempt agricultural workers from all taxes and to increase the role of long-term loans. Soft loans for the construction and modernization of livestock premises in the North and the Arctic should be granted for 20–25 years, and for the purchase of equipment – for 6–8 years.

Apparently, it is necessary to revise the corporate policy of resource companies with their desire to withdraw non-core assets from the balance of their business. It is desirable to recover subsistence agriculture within industrial enterprises, at least in the minimum amount and it should be funded from the profits of mining companies. The costs of agricultural production that are taken out of the profit should be exempt from taxes.

When substantiating the directions of improving state regulation of agriculture it is necessary to consider the role of the sector not only in the provision of food but also in addressing the issues of complex development in rural areas, the preservation of traditions, cultural and moral values, environment and natural landscape and satisfaction of recreational needs of the society. The implementation of multi-functionality implies carrying out the modernization of the agricultural sector within the framework of concepts and programs for integrated and sustainable rural development.

The term “rural development” has recently become widespread. The EU has been engaged in the development of policy in agriculture since the 1970s [6], in our country – since 2000s [2, 5, 7, 8, 11, 14].

The transition from the policy of development of the agrifood sector to rural development policy is necessary at the municipal level as well. An example of this target-oriented

management can be found in the municipal program of Usinsk urban district “Sustainable development of rural areas in 2014–2016 and for the period till 2020” dated November 28, 2013. The program consists of two subprograms: “Social development of the village” and “Agricultural development”. The amount of subsidies from the municipal budget for the implementation of the program in 2014–2016 will be 89.8 million rubles, including for the subprogram “Social development of the village” – 48.0 million rubles, and for the subprogram “Development of the agro-industrial complex” – 41.8 million rubles.

The implementation of the measures set out in the program will create prerequisites for the improvement of living conditions in rural areas, for enhancing social-engineering development, for increasing the attractiveness of rural areas for comfortable life and work, for increasing the production of potatoes, meat and milk.

Currently, the local government in peripheral areas does not have the financial base for the integrated and sustainable development of their territories. According to some scientists, the accelerated socio-economic development of rural territories in Russia can be facilitated with the use of the one-tier model of local government with a strong economic base formed at the expense of own revenues by not less than 75% [13, p. 20].

The problem of development of rural areas and of the agricultural sector, the basic branch, is complex in its nature and it requires the involvement of regional science in the study of various aspects of spatial organization of the rural economy, production, market and social infrastructure. Science needs the social order for conceptual development of

various scenarios for possible sustainable socio-economic development of the agricultural sector in rural areas.

### Conclusion

The analysis of the current government support to agricultural production allows us to propose a set of measures for its improvement with regard to the northern and arctic areas.

1. In the conditions of the North and the Arctic, due to the low profitability of agriculture, significant payback period, lack of interest on the part of private investors to finance its development, the role of the state is especially important, because it acts as the organizer, coordinator and principal participant of the technological improvement of the sector and the solution of social problems of the village.

2. The analysis of the existing financial support to the agrarian sector of the arctic and subarctic areas of the Komi Republic indicates that its volume is insufficient not only for the innovation development of agriculture, but also for curbing the decline in production. The volume of budget support does not take into account the contribution of the zone of the North to the production of wholesome food, the specifics of agricultural specialization, the level of development of transport and social infrastructure. The main burden of financial support to agricultural producers falls on the regional budget. The enhancement of profitability and investment opportunities of the agricultural production requires the increase in the amount of direct government support in 3–4 times. Boosting the modernization of industry and infrastructure in rural areas will also require the allocation of state capital investments.

3. In order to achieve early transition of the agricultural economy to a new technological basis it is proposed to subsidize it not only from the regional budget but also from the federal budget. It is advisable to direct the federal budget funds to the state support for the increase of cattle and reindeer head, volume of beef, venison and milk, and for the elimination of rural poverty.

4. Russia's membership in the WTO will require that the limitations on the level of support for "yellow basket" be removed for the northern and arctic areas that have extreme conditions for agriculture. The removal of restrictions on agriculture of the North will increase profitability, wages of agricultural workers; it will provide their employment, increase investment opportunities and

accelerate the modernization of cattle and reindeer breeding.

5. It will be necessary to enhance the role of long-term preferential loan in the modernization of the agrifood sector, to exempt agricultural organizations and farmers from taxation, to recover on a limited scale subsidiary farming of industrial enterprises and to finance it at the expense of the profit of mining companies.

6. The improvement of state regulation of agriculture is proposed to be undertaken within the framework of regional and municipal programs for the development of the agrarian sector and rural areas. Currently, the local government in rural areas of the Komi Republic has no financial basis for the integrated and sustainable development of its territories.

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