Small farms in transition economy: do they have chances to survive? Case of Armenia

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Abstract

The elimination of subsidies to the agricultural sector after the privatisation of the farmland together with the collapse of traditional markets (both sales and procurement)) in the former Soviet Union brought about an acute problem of cash necessary to buy inputs as well as to bring the produce to the market. Furthermore, the lack of assets in commercial banks and the inadequate credit policy in the country made it extremely difficult for small farmers to get credits. In this paper the situation with credit and cash availability is analysed drawing on a sample study of 62 farms in two study areas.

Keywords: transition, small farming, credit, cash, sustainability

Problem Statement

Armenia was the first of former Soviet republics to privatise the farmland in 1991. The transition period from the authoritarian planned economy to new market type of economic relations started since then and continues until now. In what environment are they farming now? Is it at all possible to tribe sustainable farms having a country average 1,4 ha land (those in the main agricultural zone, Ararat Valley have even less land barely reaching 1 ha)?

Objective

This is an attempt to analyse the credit and cash situation of 62 sample farms which are supposed to represent more than 320,000 small family farms. The work is done in the frames of a PhD study which tackles, using a holistic approach of FSA (Farming Systems Approach), the problems at farm-household level, analyses the perceptions of the farmers of the presence and discusses their perspectives and plans for the future.

Methodology

The study utilised the FSA, together with comparative descriptive statistics, to arrive at recommendations and suggestions hopefully bringing useful insights to policy makers, specialists, and to farmers themselves. SWOT analysis is integrated as a tool to discuss internal strengths and external treats of an average family farm in two study regions in regard to credit availability and use.

The study areas differ geographically (agro-climatic conditions) and in terms of market access.

The scope of discussion

The paper covers just a part of salient aspects of farm-household systems. Because of space limitations and because of the need and the importance, we found it reasonable to deviate from the initial intention to cover many other issues and here concentrate our discussion on the problem of credit and cash availability only. These characteristics, together with land use pattern, farm and family income, age, education, health aspects underline the extent and the diversity of the problems faced by family farms in Armenia.

Credit and cash availability

Credit situation

Taking credits is considered to be a quite risky business because of highly uncertain economic and political situation. This explains the very high percentage of credits used for short-term purposes like production rather than using scarce financial means for investments, hoping to get relatively quick returns to pay back the credits. The land as a collateral does not appear at all because land market does not exist and there are virtually no procedures and regulations for the sales of the farmland. Therefore, farmland is of no interest for the banks which prefer items with higher liquidity.

Table 1: Farmers' credit situation, study regions, Armenia, 1997/1998

Study areas	**Ararat Valley**	**Marginal Mountainous Region**
Number of cases	n=34	n=31
Families in debt	58,82%	31,07%
Reasons for taking credits 1\		
-Production	100%	88,24%
-Investment in the farm	0%	11,76%
Source of loan 1\		
-Relatives/friends (cash)	40%	51,35%
-Bank	60%	48,65%
Types of collateral 1\		
-House/Apartment in the city	5%	0%
-Means of production (cars, trucks, tractors, etc)	40%	29,41%
-Personal pledge	15%	5,88%
-Harvest	40%	64,75%

1US$=550 Armenian Drams
1\ The percentage is calculated only from the number of families which are in debt. At least one answer is given per family.
Source: Khachatryan (2000)

The friends and relatives are the preferred source of credits. However, their possibilities are relatively limited. Banks play quite important role in providing necessary cash, though the time period is limited to 12 months maximum with in average 16% of interest per annum which is relatively high.

Farmers complain that it is extremely complicated and time consuming for them to get loans from banks and that often they were told no loans were available when in fact there were funds (they are just scarce and are usually being given out to friends and relatives). Farmers pointed out to considerable delays in disbursements thus endangering the timely accomplishment of necessary agricultural activities. The ridiculous thing is that those who managed to get a loan should pay a part of it as, so to say, thanking fee (i.e. bribe). A farmer in one of the villages expressed his deepest disappointment that he had had to put more collateral to get a loan as others (not specified) for the same amount of the loan.

Worthwhile mentioning that the banks get the funds through the participation in a tender organised by the Ministry of Agriculture. The latter gets those funds available from international funding sources (IMF, World Bank, EBRD, etc). The procedure is far to be perfect and leaves a lot of room for misuse and fraud.

Cash situation

The analysis of the family cash balance gives the idea whether liquidity problems of the family can be met. The liquidity is defined as "the ability to meet the cash liabilities in time" (Steinhauser et al, 1989). Doppler (1991) stresses the relevance of liquidity issues for the decision-making process considering it as an important criteria for the living standard of the families.

Table 2: Cash balance (in US $) in the study areas, Armenia, 1997/1998

Study areas	**Ararat Valley**	**Marginal Mountainous Region**
Number of cases	n=31	n=31
Cash inflows		
Crop production	1158.87	382.42
Livestock production	129.73	889.90
Off-farm use of own machinery	0	0
Off-farm income	1527.27	1191.27
Loans	875.91	369.52
Total cash inflow	3691.78	2833.11
Cash outflows		
Crop production expenses	618.30	418.78
Livestock production expenses	212.82	549.98
Farm investment cost	157.75	176.42
Payment for interest rate	105.11	44.34
Household expense	1758.24	1378.96
Total cash outflow	2852.22	2568.48
Cash balance	**839.56**	**264.63**

1US$=550 Armenian Drams

Source: Khachatryan (2000)

At this point it is necessary to mention that an assumption was made that no cash remained from the previous year operations. The absolute values, therefore, are doubtful, however providing a valuable insight into the liquidity situation of the families.
Obviously, livestock activities contribute negatively to the improvement of cash situation of the families in Ararat Valley. However, the farmers prioritise the availability of high quality milk, home made cheese and butter for the household consumption. Interestingly, all of them point out the children as major argument for continuing keeping animals.
Credits taken are less in the marginal zone. This is explained not by that the families here do not need more credit but by the fact that credit institutions are overwhelmingly far in the city and the application, verification, preparation activities on both sides (the banks and the farmers) usually take considerable time and effort to bring the deal to the successful end.

The results and perspectives

It is shown that small family farms are largely of subsistent character however having good opportunities to expand into commercial operations. It is difficult for Armenian farmers to get credits. For those who have no collateral to offer, the guarantee of the state enterprise is required. There has to be a programme established which would help farmers who do not meet conventional agricultural credit criteria. This would allow to increase small family lending. Already now there are positive signs indicating to the big potential of the rural financing. According to the media (Agrolratu, 25 March, 1997), as of 1st January 1997, 400 farms in only three provinces (out of 10) have got loans up to 1000 USD (maximum for 1 year), and the payback of loans constitutes 100%. This is a fact which is extraordinary and unique to many international organisations. We advise to pay closer attention to this excellent credit behaviour of the farmers and work out more effective ways of bringing more financial means to the rural communities. We suggest developing better (probably direct from international financing sources) procedures for the banks to get necessary credit funds. While the new private commercial banks may be more inclined to lend to agriculture, the amount of loans these banks may provide do not make significant impact on the availability of credit to agriculture. Also, the way the farmers get eligible for getting loans, i.e. they have to open an account at a hefty fee as a prerequisite, has to be revised for farmers to appreciate the credit policy of banks. In this respect, the suggestions of the World Bank (A World Bank Country Study, 1995) still remain of drastic importance. According to those suggestions, the strategy for strengthening the rural financial system may be divided into several steps. Fiscal means, rather than financial institutions should be used to sustain the operation of those state enterprises having critical importance to food security, and **to support the newly established private farms.** The short term approach would be to improve the existing system of rural finance to make it a more effective instrument in channelling resources into market oriented businesses and to support the major thrust in further privatisation. The medium-term agenda is to introduce financial viability into the existing system as well as develop alternative channels of rural finance to strengthen rural financial intermediation and encourage competition The establishment of rural savings and credit societies should therefore be promoted. The long-term goal would be to develop a viable rural financial system as an integral part of the overall financial system. The reason for creating a rural financial institution stems from the realisation that farmers' needs are not being met by the existing institutions. The banks should work on building confidence of rural households to increase deposits from them. We recommend to develop constructive engagement between interested parties such as public and private organisations and farmers as soon as possible as these can foster rural development, relieve social tension, mitigate the costs from market and policy change. To conclude, it is strongly believed that the private farmers are ready for cooperation, they need support and surely they will payback the better attitude to their problems and needs by contributing largely to the rural development thus raising the welfare of rural (as well as urban) families and ultimately that of the society to a new qualitative level.

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