

Impact Assessment of Lithuanian Integration into the European Union

Impact of the Reform of Common Agricultural Policy to the Milk Producing Sector of Lithuania in the Medium-term perspective (until 2008)

Summary

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The dairy sector is one of the priority agricultural branches in Lithuania. The value of milk makes up 18,6 per cent in the structure of total agricultural output; 69 per cent of agricultural entities are engaged in production of milk.

Income from the milk sold comes to one third of the total income from sales of agricultural products. The exports of dairy products make up over 30 per cent of the total exports of agricultural and food products. Production of milk also is of social importance: income from milk makes a large part in total income of many rural residents.

In the 1997-2003 period structural changes were observed in dairy farms: the number of large-scale agricultural enterprises was declining, while that of family farms was increasing. During this period the number of very small farms keeping 1-2 cows decreased significantly. It is likely that in future farms will keep enlarging because small dairy farms being uncompetitive will not be able to meet EU veterinary and hygiene standards.

The quality of milk purchased is growing up. In 2003, milk of the best quality amounted to 79 per cent of the total amount of milk purchased, that of the first grade – 13 per cent and of the second grade – 6 per cent. Whereas in 2001 milk of the best quality accounted for 52 per cent. Average milk yield per cow during the last five years increased by 24 per cent.

The Lithuanian dairy sector has a competitive advantage (in comparison with Ireland, Denmark, Netherlands, New Zealand) due to the following indicators characterizing competitiveness: cheaper grass fodder (favorable climatic conditions for cultivation of grass crops) prevail in feeding ration, good conditions of environment protection, low cost price of milk production, cheap labour force, low milk prices.

Lately positive changes increasing competitiveness of production of dairy products are observed. Concentration and net profitability of the Lithuanian dairy industry reached EU level. The imports of dairy products are rather small; according to the RTA index competitive advantage of milk and key dairy products is higher.

In comparison with other countries, economic indicators the Lithuanian dairy sector show the following weaknesses of competitiveness:

- Unreasonable structure of agricultural entities, prevail small farms with low investment capacity, many dairy farms are still in the making stage;

- In Lithuania productivity of cows is about 35 per cent lower than EU average;
- Fat and protein content in Lithuanian milk is lower than in EU countries and New Zealand;
- In Lithuania seasonal milk production is to a rather considerable degree (milk supply in summer period is twice higher than in winter);
- Veterinary and hygiene standards are not implemented in some dairy farms, milk quality is insufficient;
- Low profitability do not encourage dairy farms to expand production of milk, there is a lack of funds for modernisation and the increase of efficiency;
- Dependence of Lithuanian dairy industry on changes of the market of balance dairy products (in Lithuania about 58 per cent of the total milk purchased are processed into balance dairy products);
- The enterprises of Lithuanian dairy industry, in comparison with dairy enterprises of other competitive countries, are rather small, specialisation in production of dairy products is not sufficient, a level of production capacity utilisation is about 70 per cent;
- Labor productivity is insufficient (in comparison with Ireland, Denmark, Netherlands, New Zealand), in Lithuania the amount of milk processed per employee is up to 10 times lower.

The growth of the Lithuanian dairy sector will depend on openness of country's economic system and integration into world markets. The growth of total country's economy will have positive influence on the increase of production scope of dairy products, and Lithuania's membership in the EU makes market conditions better.

EU membership provides for regulation measures of the dairy market: intervention purchases of butter and skimmed milk powder, subsidies for private storage, exports, skimmed milk for animal fodder, support for butter used in confectionery, milk and dairy products consumed at educational institutions. The application of these measures will influence positively all participants of the dairy market as well as the balance of dairy products' demand and supply.

Implementation of market regulation and structural policy measures enables to sell Lithuanian dairy products in prices higher than relative world prices. The gap between seasonal prices will be reduced.

EU membership provides the Lithuanian dairy sector for support from EU structural funds to improve infrastructure, to develop information and consulting services.

Implementation of CAP measures applied up to 2006 in dairy farms will make more favorable conditions to increase profitability in large farms and small semi-subsistence farms. The dairy farms will receive direct payments for the area of fodder crops used for milk production, support for semi-subsistence farms, and national support for quantity of marketable milk. Including this financial support net cash income for 1 tonne of milk sold will increase to 259 Lt in small farms, and to 242 Lt in large farms; the share of financial support in net cash income will make up 83 and 68 per cent, respectively.

The dairy farms in less-favored areas will get compensatory allowance for the area of fodder crops. This support fully covers higher costs of milk production due to lower yields of fodder crops in these areas. Support to farmers in less-favored areas will smooth different farming conditions and milk producers will have equal conditions to adjust to EU standards in production of marketable milk.

Small milk producers (2-3 cows) due to small production scope and part-time employment will not be able to accumulate enough funds to develop activity, which meets quality and hygiene standards. Therefore a part of these farms will be not commercial and will produce only for own needs. Implementation of early retirement measure and possibility to adjust work in farm and other rural economic activities will be important solving social and economic problems of small milk producers.

Financial support paid under CAP measures implementation scheme for farm economic strengthening and equalization of farming conditions, and expected higher producer milk prices cover the increase of costs for milk production, make more favorable conditions to large and small semi-subsistence dairy farms to strive for effective production and to increase competitiveness.

The dairy sector will remain an export-oriented agricultural branch. Due to favorable changes in trade regime for the exports of dairy products, expanding markets, increasing scope of production of milk and dairy products and competitiveness of the sector, the growth of average annual export of processed dairy products in 2003-2008 should reach about 8 per cent, the exports will increase by 41 per cent and will come to 60 per cent of the total production.

In 2004-2008 production of milk should increase by 14 per cent, and amount of milk purchased by 38 per cent, per capita consumption of dairy and dairy products over 7 per cent (average annual growth of consumption 2 per cent). The structure of consumption of dairy products should change: dairy products of higher quality and wider assortment will be of greater demand.

Primary production of should be determined by the growth of cow productivity, which average annual growth in 2004-2008 will reach 3,4 per cent; according to prognosis, in 2008 average milk yield should be 4650 kg or by 12 per cent higher than in 2004.

The amount of milk purchased will increase every year on average by 7,5 per cent and in 2008 its share in total amount of milk produced will make up about 74 per cent or will be by 16 percentage points more than in 2003. In 2003-2008 the share of milk consumed in households and directly sold to consumers will decrease; average annual change in the amount of milk used for animal feed will be not significant.

It is prognosticated that in 2008 per capita consumption of milk and dairy products will increase by 12,6 per cent compared to 2003 and will reach 323 kg. Although the growth of consumption of processed dairy products is insignificant, the consumption of natural milk in households and directly sold to consumers will decline.

The changes in prices of milk will be determined by country's economic situation, purchasing power of population and prices of relative products in other EU countries. It is prognosticated that in 2008, compared to 2004, prices of all milk and dairy products will increase as follows: milk by 40 per cent, and cheese by 26 per cent, butter by 31 per cent, skimmed milk powder by 12 per cent.