

## THE CASE FOR FOREIGN OWNERSHIP OF FARMLAND IN POLAND

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The present law on land ownership in Poland has been in force since 1920. This law allows foreign interests to buy only small parcels. Larger plots can be acquired only with permission from the Ministry of Interior, which needs to consult every such decision with the Ministry of Agriculture. Consequently, this regulation makes foreign purchases of farmland very difficult. The accession agreement between Poland and the European Union (EU) allows for the preservation of the existing limitation for another 12 years.

The justification for the exclusion of this particular asset from the EU laws protecting free movement of labor and capital within the Union's boundaries is its alleged low price. According to the popular view held in Poland, local farmland is very cheap and it will take about 15 to 20 years for the price of this resource to approach the average EU level. Successive Polish governments have shared this opinion for many years. Indeed, the average price of farmland in the EU is 7.5 times higher than the average price of this asset in Poland. However, the difference varies greatly: farmland is 30 times more expensive in the Netherlands, 10 times more dear in western parts of Germany, but only twice as costly in former East Germany.

The purpose of this article is to show that there is no good justification for this prohibition either on economic or equity grounds and that the Polish economy suffers as a result of this restriction. Agriculture is a very important industry, but this sector has greatly underperformed the rest of the economy since 1989. Foreign participation in farm ownership is a quick and easy way to increase the price of farmland and to reinvigorate this industry.

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## Agriculture and the Polish Economy

Agriculture is still a vital sector of the Polish economy and a large segment of Polish society depends on this industry. The data in Table 1 point to a substantial decline in agricultural production over the period 1990–2002. As a result, the share of agriculture in the GDP declined precipitously. Table 1 also points to a considerable drop in the standard of living of all those who are professionally active in this sector. Clearly, the post-communist transformation failed to bring about positive changes in Polish agriculture.

TABLE 1  
ECONOMIC PERFORMANCE OF POLAND

Variable	1990	2002
Growth		
GDP	100.0	146.5
Industrial production	100.0	177.4
Agricultural production	100.0	91.1
Share (%)		
GDP generated by agriculture	8.3	2.7
Agricultural population	23.6	18.0
Economically active in agriculture	27.5	20.7

SOURCES: GUS (2003b, 2004), FAO (2004).

Ironically, under communism agriculture was the only key industry with a majority of assets privately owned. Unlike other sectors that were subject to rigid central planning, agriculture possessed a large number of people accustomed to risk-taking and familiar with the workings of the market mechanism. Hence, at least in theory, this sector should have led the economic revival rather than trailed it.

Macours and Swinnen (2000a) note that economic reforms and rapid growth in China and Vietnam were preceded by reforms in agriculture. They also report that in Albania, following the demise of communism, gross agricultural output “has grown more than 10 percent annually on average” (p. 173) for the first four years. Moreover, they find that the only factor that had a positive influence on agricultural output in Central and Eastern European Countries (CEECs) is restructuring of the industry.

The shift to individual farming is estimated to have a very strong positive effect on total output. However, the disruption associated with this process substantially decreased the overall impact of the movement toward individual farming. Since individual farming in

Poland was prevalent even under communism, the disruptive effects were not present. Nevertheless, unlike in Albania, or earlier in China, agricultural output in Poland fell considerably. However, after the fall of communism, Polish agriculture was to some extent sheltered from international competition. In particular, the restriction on foreign ownership of land prevented the restructuring of the agrarian structure and has hindered the process of transformation of agriculture.

### Adjustment Process

Calculations concerning the speed at which prices of farmland in Poland might catch up to those prevailing in the EU are based on the assumption that the Polish market is closed to foreign buyers. If foreign participation were allowed, prices would rise as demand for farmland increased. The magnitude of the increase, of course, depends on the price elasticity of supply. Usually the supply of unimproved land (and farmland is relatively unimproved) is assumed to be fixed in quantity (i.e., price inelastic). There are no precise empirical data on the price elasticity of supply of farmland in Poland. However, the price of urban land, which can be easily sold to foreigners, has greatly appreciated in real terms since the fall of communism. A study by Łucka-Matysik (1999) shows that real estate prices in Krakow, a major city in southern Poland that attracts substantial foreign investment, rose tremendously in real (dollar) terms between 1993 and 1998. During that period the average price of a building-plot in the prime area of the city rose more than five times (from \$14.15 to \$72.99 per square meter). In the least attractive part of Krakow, plot prices more than doubled over the same period.

Since there is no reason to believe that the supply of land in Poland is price-elastic, an increase in demand (resulting from foreigners rushing to buy cheap Polish land) should lead to a large increase in the equilibrium price. Actually, the greater the foreign interest in acquiring inexpensive Polish farmland, the greater is the price appreciation. This implies a relatively quick adjustment process. So, if farmland in Poland is indeed an attractive acquisition target, then it will take much less than 15 or 20 years for the price of this asset to appreciate to an average EU level once foreign participation in the market is allowed.

### Demand for Farmland

The fundamental question is whether or not the relatively low price of farmland in Poland is a result of market imperfections or other factors. In other words, is farmland in Poland really that cheap?

In competitive markets, asset prices depend on the value of discounted future cash flows—that is, on the net present value criterion. This is also true of farmland. For instance, Roche and McQuinn (2001) show that the price of farmland in Ireland varied significantly over the years 1911–96. Like financial assets, land could be a subject of speculation leading to a major boom-and-bust cycle. Thus, if Polish soil generates huge cash flows and if the current market price of farmland fails to fully reflect the net present value of future cash flows, then arbitrage activity should set in and the demand for land should increase. A rise in demand, in turn, should cause the price to go up. But Poles have shown a lack of interest in purchasing farmland.

In 1992, the Polish government put up 230,000 hectares of state-owned farmland for sale, but the state managed to sell only 14,000 hectares and to lease an additional 75,000 hectares (Rowinski 1994). Overall, in the period 1990–97, the share of land in individual use increased only slightly: from 77 percent to 82 percent. Over the same time, private ownership of land increased from 4 percent to 100 percent in Albania, and from 5 percent to 95 percent in Latvia (Lerman 2001). Not surprisingly, Lindemans and Swinnen (1997: 273) observed that “compared with other CEECs, the privatization of agricultural assets in Poland has lagged behind.” The authors attribute this development to low profitability of agricultural production, scarce credit, and a mismatch of regional demand and supply. The last factor is a result of the fact that most of the state-owned land is located in the North and West of the country, territories that before World War II belonged to Germany, while family farms predominate in the rest of Poland.

Unlike other former Soviet-bloc countries, Poland retained private ownership of land. Consequently, there should be no shortage of people used to buying farmland and developing it. The lack of interest in buying land most likely reflects a low level of profitability related to investing in this asset.

## Productivity of Polish Farmland

The rate of return on farmland is, among other things, a function of its productivity. In Poland, the productivity of land is poor. First, natural conditions are not better than those prevailing in most of Europe. Poland enjoys neither soil of superior fertility nor a better climate than that found in most regions of both Eastern and Western

Europe<sup>1</sup>. Among the CEECs, Poland is the northernmost, with the least sunshine and the coolest average temperatures. Thus, in terms of climate and fertility, Poland has no advantage in relation to EU countries.

It is evident from Table 2 that average crop yields in Poland are much lower than those for the EU, except for primary oilcrops, and much lower than those for neighboring Germany (for all products). Besides, crop yields in Poland are similar to average yields in other CEECs (except for primary oilcrops and potatoes) in spite of the greater than the region's average use of machinery and fertilizers (see Table 3). It is also worth noting that during the 1990s the productivity gap between Eastern and Western European agriculture further increased. Given the above, it should not come as a surprise that in 1989 Poland had a surplus in agrofood trade of \$448 million, but by 1996 the balance turned into a substantial deficit of \$1,218 million (Banse 2000).

TABLE 2  
CROP YIELDS IN EUROPE  
(Hectograms/Hectare)

Crop	Year	Poland	CEECs	Germany	EU (12)
Cereals (Total)	1989	32,182	37,664	52,036	46,645
	2002	32,351	34,028	62,515	57,631
Wheat	1989	38,542	41,574	56,815	48,693
	2002	38,388	32,351	69,056	58,514
Rye	1989	27,325	27,898	38,770	33,763
	2002	24,109	24,177	50,330	44,622
Potatoes	1989	185,048	165,710	264,966	265,398
	2002	190,172	166,472	404,526	366,518
Sugar Beets	1989	340,077	348,765	449,408	528,665
	2002	387,789	397,933	583,074	615,788
Oilcrops (Primary)	1989	9,878	6,206	12,133	6,282
	2002	8,405	6,202	11,070	6,833
Rapeseed	1989	27,821	26,712	32,420	29,844
	2002	22,797	20,727	29,669	30,503
Strawberries	1989	47,762	49,439	90,584	153,031
	2002	39,814	44,081	114,583	200,790

SOURCE: FAO (2004).

<sup>1</sup>The Food and Agriculture Organization (FAO) classifies Albania, Bulgaria, Hungary, Poland, Romania, the Czech Republic, Slovakia, and Yugoslavia and its successor states as Eastern European countries. This article uses data on the 12 nations that constituted the European Economic Community in 1989, denoted EU (12), as a proxy for Western Europe.

TABLE 3  
AGRICULTURAL MACHINERY AND FERTILIZERS IN EUROPE

	Year	Poland	CEECs	Germany	EU (12)
Harvesters and Threshers (hectares/unit)	1989	242.7	389.5	116.5	283.7
	2001	189.6	388.7	126.2	309.8
Tractors (hectares/unit)	1989	16.3	25.6	11.3	21.0
	2001	14.1	28.0	16.5	20.9
Total Fertilizers (kilograms/hectare)	1989	176.0	135.3	254.3	145.6
	2001	85.6	56.1	153.4	110.3

SOURCE: FAO (2004).

Also studies conducted by the World Bank and the European Commission (EC) show that the performance of Polish agriculture has not been very impressive (Davidova and Buckwell 2000). Indeed, the World Bank study, which included Estonia, Bulgaria, Hungary, Latvia, Romania, Poland, and Slovakia, found that for the years 1994–96, Poland had the lowest productivity—agricultural workers produced only \$1,359 per employee (in 1987 U.S. dollars)—compared with \$6,266 per worker for Estonia, which had the highest productivity. Moreover, Poland’s agricultural output was only \$366 per hectare (the second lowest), while Estonia’s output was \$526 per hectare. The EC study measuring gross agricultural product (GAP) per employed in 10 former Soviet block countries in 1996 paints a slightly brighter picture. Poland, with a GAP per employed of 1,574 ecus is ahead of Latvia, Romania, Lithuania, and Bulgaria (which placed last with a GAP per employed of 1,170 ecus), but trails badly behind Slovenia (the most productive country with a GAP per employed of 11,475 ecus, more than seven times that for Poland), Hungary, Czech Republic, Slovakia, and Estonia (a GAP per employee of 4,054 ecus).

The good reputation that Polish agriculture enjoys is a legacy of the past. During the communist period, Poland was the only country in the Soviet bloc that allowed private ownership of land. However, what was a relative advantage at that time may prove to be the Achilles’ heel today. In other countries the communists created huge farms, while Poland retained the old, pre-World War II agrarian structure. Consequently, as late as 2002, 13 years after the fall of communism,

the average size of a private Polish farm was only 7.4 hectares (about 18 acres) (GUS 2003a).

In the former Soviet Union, the process of decollectivization is resulting in larger private farms. For instance, the average size of a private farm in Russia is 40 hectares, in Ukraine 20 hectares, and in the Baltic States 10–15 hectares (Lerman 1995). Also, the size of individual farms in Central and Eastern European countries increased to 5–20 hectares, from about 0.5 hectares (Lerman 2001). Liefert and Swinnen (2002) note that Hungary and the Czech Republic recorded the highest increases in labor productivity in agriculture among the transition economies in the period 1990–98. They credit this phenomenon with the fact that “the large socialist-era farms in these two countries have turned into private, large-scale corporate enterprises” (p. 24). On the other hand, labor productivity in Poland stagnated over those same years. This is not surprising, because an earlier study (Macours and Swinnen 2000a) found that privatization leading to the creation of small farms had a negative impact on production efficiency.

A study of North American agriculture by Hallam (1991: 168) concludes that “most empirical work of the last 40 years has identified few economies of size for agricultural production firms at levels much above those of the average firm”—in other words, the cost curve is L-shaped.<sup>2</sup> The average size of a crop farm in North America is about 500 acres. As mentioned previously, the average farm in Poland is some 28 times smaller than that. The disparity in dairy farming is even greater. Hallam considers a dairy farm small if it has about 100 cows. In Poland the average dairy farm has about two cows (Gorton, Buckwell, and Davidova 2000). Although in Europe farms are, in general, smaller than in North America, still the average farm in Poland is about 3 times smaller than the EU average and 10 times smaller than that in Germany. In sum, Polish farms are very small compared with those in the West, and farmers could decrease the cost of production by increasing the acreage of their holdings.

The small average size of farms in Poland forces the preservation of obsolete techniques and of outdated organization of this industry, which prevents the capture of benefits resulting from economies of scale. The fact that Polish farms are very small on average could help explain the low price of farmland. For instance, Maddison (2000)

<sup>2</sup>The above is true for farming with seasonal factors present, for instance in crop farming, because seasonal factors increase risk. However, in areas of agriculture where the impact of nature is eliminated—for instance, in feedlot cattle, hogs, and poultry—economies of scale persist, and factory-like production dominates (Allen and Lueck 1998).

found that in England and Wales the highest prices are paid for very large plots of farmland (in the range of 1,000–2,000 acres). As noted in Table 3, after the fall of communism, Polish farmers greatly increased investment in physical capital. Consequently, 12 years after the fall of communism, Poland, on average, was better endowed with tractors, harvesters, and threshers than EU countries. Amazingly, a Polish tractor has to work fewer hectares than its German counterpart. However, this advantage is not reflected in productivity because the average size of Polish farms is far below the optimal level.<sup>3</sup>

## Government Policies

Agriculture is the most subsidized and protected industry in the world. The industrialized world expends more than \$300 billion a year on agricultural subsidies (Wolfensohn 2001). Poland's western neighbor, the EU, supports agricultural producers the most. According to the OECD (2003), in the period 2000–02, the EU spent on average \$103.8 billion, or about \$14,000 per individual economically active in agriculture, in total support to this industry while the respective numbers for Poland stood at \$2.3 billion and \$530. Clearly, government policies, in particular the degree of financial support, affect the level of profitability in agriculture.

CEECs liberalized the market for agricultural inputs and outputs following the demise of communism. Given the level of government support that other producers enjoyed, this laissez-faire policy resulted in a huge deterioration in agricultural terms of trade for the entire region (Macours and Swinnen 2000a). The worsening of agricultural terms of trade was most dramatic in Romania, Poland, and Bulgaria. Consequently, incomes of farmers and agricultural output declined

<sup>3</sup>The question of optimal farm size for Poland is beyond the scope of this article. Existing research, however, provides some guidance. For instance, Hughes (2000) points to significant economies of scale for private farms in all categories (all products, as well as in crop and livestock production) in the Czech Republic. In that country, the smallest private farms (5–25 hectares) have by far the lowest total factor productivity (overall and crop) while the largest (500–1,000 hectares) have the greatest. However, the situation in Hungary points to a different phenomenon. Here, total factor productivity in crop production is highest for the smallest (5–25 hectares) private farms. However, very large private farms have the greatest productivity in livestock and overall. Hughes explains the apparent diseconomies of scale for crop production with the fact that small-scale farming was allowed under communism and, therefore, farmers operating small farms have more experience than those operating new, large ones. Another important issue is the size of the small farm sample, which included just six farms. Overall, the prevailing view is that private, medium-size, family farming provides the best long-term solution to CEECs agricultural problems (Turnock 1997; Sarris, Doucha, and Mathijs 1999).



substantially throughout the area. A tremendous decrease in support to farmers combined with foreign exchange fluctuations resulted in a negative (about 20 percent) producer subsidy equivalent (PSE) for Poland in 1990 (Hartell and Swinnen 2000). The dramatic decline in output and profitability of agricultural production led to the reintroduction of subsidies and other forms of protection. Consequently, Hartell and Swinnen found that in 1992 the PSE turned positive (at about the 20 percent level) and has been fluctuating around that level ever since. In the second half of the 1990s Poland made efforts to align its policies toward those of the EU, but still the degree of protection remains well below that of the Union. Hartell and Swinnen (2000) estimate that the average level of protection in the EU is about twice as high as in Poland.

Valdés (1999), using a different methodology (he calculates PSE as a percentage of agricultural GDP, as opposed to the value of output), estimates that the total PSE for Poland varied between 11 and 18 percent for the period 1995–97. On the other hand, the total PSE for Germany varied between 64 and 65 percent over the same time. According to the study, Turkey, a country that aspires to EU membership, had total PSE between 35 and 42 percent for the years 1994–96. Valdés also noted that in Poland real producer prices for the most important agricultural products declined over the years 1995–97, while they rose in Germany. Moreover, in Poland real prices varied greatly from year to year, increasing the riskiness of farming. Overall, Valdés (1999: 269) concludes that “agricultural policy in these transition economies remains unfocused and, as a result, falls short in terms of contributing to the competitiveness of the agricultural sector” and “a striking finding is the role of government price and trade policy in exacerbating price instability.”

The asymmetry between the level of government support for agriculture in Poland and in the EU did not disappear in May 2004, when Poland became a member of the Union. The Common Agricultural Policy will be phased in over a period of 10 years. In the first year, Polish farmers will receive direct support from Brussels only equal to 25 percent of what their western competitors are getting. The Polish government could add another 30 percent, thus increasing the total to 55 percent. However, import barriers on foodstuffs will be dismantled immediately and, consequently, Polish farmers may suffer deterioration in their overall economic situation.

In sum, it is not in the least surprising that the price of farmland in Poland is lower than in Western Europe. The price differential reflects the huge disparity in productivity between Poland and the EU rather than market imperfections. To make Polish agriculture

competitive with that of the EU, this sector has to undergo massive consolidation of land to increase the average size of farms. To accomplish this a great deal of financial capital is needed. So far, neither the domestic private sector nor the Polish government has made such a commitment.

### Foreign Investment and Productivity of Land

Given the above, a logical conclusion is that the capital should come from abroad. This would improve the situation for three reasons. First, foreign interests would buy land to make money. The only way to capitalize on this opportunity is to make Polish agriculture more efficient. Foreign investment brings into the host country not only fresh financial capital but also new methods of production, new technologies, and improvements in organization and management techniques. There are no patents or copyrights that could prevent local producers from duplicating more advanced techniques and better organizational methods from foreign farmers.

Second, Polish peasants would be better off with foreign competition. If foreigners rushed to buy Polish farmland, the price of properties would increase. With rising land prices, local farmers could leverage their landholdings more easily and could acquire additional acreage and more inputs. Ironically, an end to the limitation on foreign landholding in Poland would provide Polish farmers with more financial capital.

Finally, it is fair to assume that Polish landowners behave in a rational manner. Therefore, individuals are likely to expect that the price of farmland will increase with the end of the current restriction. For this reason, marginal producers are reluctant to dispose of their property and leave the industry. This inertia obstructs the process of land consolidation and the establishment of a more efficient agrarian structure.

In general, foreign investment forces local producers to become more competitive. On the other hand, the policy of preventing foreigners from acquiring land inhibits transformation of Polish agriculture. Because agriculture is a very important segment of the Polish economy, overall economic performance suffers as well.

### Economic Sovereignty

It is argued that small, less-developed nations may find it difficult to bargain with multinational firms. Simply, in many cases, global players wield much more economic power than small countries.

Although the Polish economy is not among the smallest, nevertheless some multinational firms have global sales much larger than the Polish GDP. Hence, it may be appropriate to discuss the question of economic sovereignty.

However, it is interesting to note that Polish governments have not seen any threat to national interests from transnational firms acquiring local industrial firms and banks. As of 1999, foreigners controlled 70 percent of the banking industry and 35–40 percent of manufacturing (Poznański 2000). Global players assumed a near monopolistic position in certain sectors, for instance in the papermaking industry. On the other hand, foreign acquisition of farmland is portrayed as a risk to national interests.

Moreover, Poznański (2000) estimates that, on average, the Polish government sells assets to foreigners at prices ranging from 7 to 9 percent of their fair value. However, it is highly unlikely that farmland could be sold at such a huge discount because more than 82 percent of the acreage is in private hands, and market forces have been operating in this industry even before the collapse of communism.

Overall, economic sovereignty is best assured with competitive markets rather than with arbitrary regulations. All over the world production of raw agricultural products is competitive. Given the size of Polish agriculture, it is hard to conceive that foreign interests could acquire enough land to monopolize the output of raw food. However, monopolization is much more likely to occur at the food-processing stage. As mentioned earlier, foreign ownership of industrial firms, including food-processing facilities, is not forbidden. Likewise, foreign-owned firms are not barred from offering inputs and services to Polish farmers.

If the Polish government was interested in protecting local producers and consumers from potentially unfair foreign competition, then the focus should be not on landholding but on later stages of the production process and on distribution, as well as on the provision of inputs. Similarly, if Polish authorities were concerned with the welfare of the nation, they would first allow the sale of land to foreigners and would allow the disposition of industrial firms only after their fair market price is determined.

Market forces would also aid Poland in containing the alleged threat of Germans repopulating territories that belonged to Germany before World War II. If many Germans preferred to leave their homeland to settle in the former German territories, then the price of land would shoot up in these regions. Consequently, a natural economic barrier to German colonization would arise. Indeed, market forces would protect Polish national interests better than any legal obstacles.

## Equity Issue

The state may be entitled to limiting property rights when it comes to protecting vital national interests. However, in Poland industrial companies across the entire economy are being sold to foreigners, and even the privatization of arms producing companies with the participation of foreign firms is being contemplated. Similarly, real property in cities could be sold to foreigners without significant restrictions; only farmland is being singled out as an asset of strategic importance. Consequently, a very serious equity issue arises.

As pointed out, foreign participation in the urban real estate market over the last decade helped drive real prices upward. Today, real estate in cities is by no means perceived as cheap. This is not true of farmland, according to all major political forces in Poland. If this is indeed the case, then all peasants who sell land while the restriction is in place dispose of their property at a price that is below what could have been obtained if foreigners were allowed to enter the market for farmland. In other words, farmers are forced to sell their land at prices that fail to reflect the asset's full potential value. But, no one is compensated for the loss.

In sum, the state's restriction on the sale of farmland creates a high opportunity cost to potential sellers of this asset. National interests do not justify this limitation, but the government fails to make up for the loss. Hence, we have to conclude that peasants are being discriminated against. Their freedom to sell property is severely restricted while owners of other assets can dispose of their holdings at will. Either the state should compensate farmers for this hardship, or the control should be lifted as soon as possible.

## Strategic Considerations

History could also aid in predicting the future of Polish agriculture. Poland's cultural "golden age" and the period of the nation's greatest economic and military might took place between the middle of the 16th and the middle of the 17th centuries. During that period the demand for grain, as well as its price, rose a great deal in nations that first introduced early manufacturing techniques, especially in The Netherlands. Poland's agriculture-based economy was fortunate to participate in that boom. However, beginning with the second quarter of the 17th century Polish exports found a very tough competitor, namely Russia. The cost of grain production was much lower in Russia, and over time Russian exports crippled demand for Polish grain.

As a result, the entire Polish economy entered a very severe and protracted crisis.

So far, post-communist Russia and Ukraine, another potential low-cost producer of foodstuffs, have failed to make significant efforts to restructure their agriculture. To a large degree, both nations have preserved the old, communist-style, inefficient system of farming (Thiesenhusen 1995, Lerman 1999). However, it is reasonable to assume that the moment these countries reform agriculture—especially if they allow widespread private ownership of farmland—the situation would change dramatically. For instance, Liefert and Swinnen (2002) agree that Ukraine and Russia (especially the southern European part of the nation) have the potential to become major producers and exporters of foodstuffs.

The present situation in those nations is a result of political and economic factors. The level of economic activity declined precipitously in both countries in the period 1989–98. Consequently, real producer prices also dropped dramatically. For instance, the price of wheat in Ukraine declined 69 percent in 1995, 20 percent in 1996, and 10 percent in 1997 (Valdés 1999). Certainly, the recession and the collapse of real producer prices must have hindered agricultural restructuring. Those events must have especially diminished interest in private ownership of farmland, and must have adversely affected output as well.

Because of economic shocks and the very slow progress in the restructuring of agriculture, the U.S. Department of Agriculture expects the former Soviet Union (FSU) to become only a medium-level grain exporter in the next 10 years (Liefert et al. 2002). Weyerbrock (2001) is even more pessimistic and predicts that the FSU will remain a net importer of agricultural products.

However, in an earlier extensive study Tyers (1994) speculated that the FSU would have attained a net cereal surplus of 30–50 million tons per year by the late 1990s. No doubt that prediction was based on the assumption that the dissolution of state and communal farms in Russia would result in dramatic improvements in productivity. This was by no means a baseless hypothesis, because under communism small household plots that accounted for about 3 percent of total farmland produced more than 25 percent of total agricultural output (Binswanger and Elgin 1998).

Tyers assessed the potential increase in productivity of cereals at between 10 and 50 percent. Much higher increases were expected for other major agricultural products, for instance, 100 percent for milk output per cow. The author also cites a 1991 Euroconsult survey that estimated losses in the Soviet distribution system for the years 1986–

90 at “14 percent for meat, 28 percent for grain (compared, for example, with 2 percent for the United States), 33 percent for milk, and more than 50 percent for potatoes” (Tyers 1994: 20). Liefert and Swinnen (2002) explain the overly optimistic forecasts with the following factors: the underestimation of the degree of support to agriculture under communism, too high expectations concerning productivity improvements, and the overlooking of the impact of poor infrastructure on transaction costs.

In 1978 China began to reform its economy and since then the country has experienced rapid growth. The reforms began with the abandonment of communal farming. Following the switch to household-based production, the average rate of growth per year in agriculture reached 7.73 percent in the period 1978–84 and continued at 5.81 percent rate during the next decade. It is especially noteworthy that grain production in land-scarce China rose from 305 million tons to 467 million, or 53 percent, over the period 1978–95 (Lin 1998). Both Russia and Ukraine are land-abundant and, therefore, it is reasonable to expect a substantial increase in agricultural production, particularly of grains, in these two countries if their governments adopt laws and policies conducive to the development of private enterprise in this sector. Macours and Swinnen (2000b) argue that the enormous divergence in the rate of growth of agricultural output between China and Russia is a result of two factors. First, in China agricultural terms of trade improved, while in Russia they greatly deteriorated. Second, China was quick to allocate property rights and improve the organization of production in this sector; Russia, on the other hand, failed to adopt such reforms.<sup>4</sup>

In sum, Polish agriculture faces more efficient and highly subsidized competition from EU producers. In the future, Polish agriculture could also be challenged by low-cost production from the East. Poland has no natural resources of comparable quality to those that Russia and Ukraine enjoy. Similarly, the Polish government is unable to match the financial resources of the West. Hence, strategic considerations point to Poland’s diversifying away from agriculture rather than specializing in the production of raw food and protecting the nation’s interests in this area at any cost.

<sup>4</sup>An excellent overview of the impact of protection of property rights on economic development can be found in O’Driscoll and Hoskins (2003).

## Conclusion

Owners of farmland in Poland face a legal restriction on their freedom to sell property to foreigners. This regulation can neither be justified on the basis of efficiency nor on equity grounds.

The argument that the legislation in question prevents foreigners from taking advantage of low prices of farmland in Poland has no foundation. First, the low price of farmland is a result of its poor productivity. The primary reason for low productivity of agriculture is the small size of the average farm that makes capturing potential economies of scale impossible. Second, an end to the restriction would bring in additional buyers, thereby increasing the demand for farmland and, consequently, its market price. Moreover, widespread expectations of a surge in land prices would materialize and inefficient and marginal landowners that now are unwilling to sell land because of its alleged low price would have no excuse to procrastinate and would leave the industry. Thus, the process of land consolidation and the restructuring of this important industry would gain momentum. Moreover, higher land prices would improve the creditworthiness of more efficient producers. This, in turn, would allow such peasants to acquire more land and better inputs. Hence, productivity of land would increase.

Furthermore, foreign investment that could take place in the absence of the present limitation would contribute to the modernization of agriculture. Local farmers would then have an incentive to emulate more efficient methods of production and, thus, management and organization of the industry would improve.

The sale of farmland does not imply loss of national sovereignty. Just the opposite, foreign ownership of land would speed up the transformation of this important industry and, therefore, improve its competitive position. A strong agriculture improves overall economic performance and, in this way, increases national economic sovereignty.

Also, current legislation effectively discriminates against owners of farmland because the restriction keeps the price of this asset at an artificially low level. This fact imposes a serious opportunity cost, especially to those who dispose of farmland, but the state offers no compensation for the forgone profit. In sum, economic reasons and the principle of equity require a quick end to this unfair treatment of farmers.

The Polish example offers important lessons to other former Soviet bloc nations that adopted similar restrictions on foreign ownership of land after 1989. This is especially true for countries like Bulgaria and

Romania that chose to return farmland to pre-World War II owners, thereby recreating an agrarian structure resembling that of present-day Poland.

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