Generational Change in Family Farms and the Situation of Arable Land, as a Factor of Production, in Hungary

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Abstract: Family farms have been the cornerstone of rural society for centuries in Hungary. They provide significant contributions to the rural population and strengthen social and cultural traditions. From an agricultural point of view, Hungary has excellent potential, both because of its climate and its location. This is why agriculture has been the country's key sector for centuries. Even today, it still plays a significant role, but in terms of competitiveness and development, it falls short of the level that could be expected regarding to its capabilities. According to the 2020 agricultural census in Hungary, 216,000 farms are managed on nearly 4.922 million hectares. A substantial proportion of these farms are family farms and a significant share of the land as a natural resource is owned by them. My study – based on secondary research – deals with a major problem in Hungarian agriculture: Generational Change. In Hungary, there is currently, no tradition of farm transfer, but the issue of generational change, is becoming an increasingly pressing problem, for the Hungarian agricultural economy. In parallel, I analyze statistical data on the relationship of family farms with arable land, one of the most important and limited natural resources of the sector. The results show, that it is essential for the long-term survival of family farms, that the land owned and used by the farm, remains in the same hands and is not fragmented. Successful generational change is therefore, also crucial for land use. Measures taken in the past and in the period ahead (e.g., targeted support under the Common Agricultural Policy Strategic Plan 2023-2027 or Act CXLIII of 2021) can help to ensure a successful generational transition and the preservation of land.

Keywords: generational change; family farm; arable land

1 Introduction

Family businesses are key players in the economies of both developed and developing countries. They contribute significantly to GDP and play an important role in employment.

Family farms, which are enterprises in the agricultural sector, have been a cornerstone of rural society for centuries. They make a major contribution to rural population retention, play a key role in employment and reinforce social and cultural traditions [1]. Despite this, the number of family farms is decreasing across Europe. The reasons are complex.

Farmers are struggling to cope with the problems of climate change, that of low viability, changing farm and agricultural holding structures and finally, successful generational change. Problems with farm viability and the lack of innovative farming practices often play a key role in succession decisions, preventing older farmers from passing on the farm [2-4].

In addition, data from the 2010 General Agricultural Census (GAC) already pointed out that the proportion of older farmers is much higher than that of young farmers, i.e., the number of young farmers entering the sector cannot replace the number of older farmers leaving it. The lack of sufficient replacement could threaten the survival of farms [5].

There is currently no tradition of farm transfer in Hungary, but the issue of generational change is becoming an increasingly pressing problem for Hungarian agriculture. For years, professional organizations have been calling for creating better conditions to support successful generational change. As a result, the Act CXXIII of 2020 on Family Farming [6] came into effect on 1st January 2021.

The primary aim was to simplify the new forms of agricultural production that would be created under this law, which is increase the competitiveness of farmers and promote generational change.

2 Family Farms

Consequently, we will review the past and present situation and the future challenges of family farming.

2.1 Family Farms in the 2nd Half of the 20th Century

After the Second World War, nationalization and collectivization of agriculture began in Hungary. Following the establishment of agricultural cooperatives, backyard farms were created.

Between 1957 and 1959, the political leadership sought to reorganize the cooperatives that had been dissolved during the revolution. After the reorganization of agriculture, large farms farmed 94% of the agricultural area and produced 2/3 of agricultural output.

At the beginning of the 1960s, there were 270 state farms, 4200 producer cooperatives and more than 400 specialized cooperatives. Later on, the cooperatives were merged, resulting in 132 state farms, 1338 producer cooperatives and 61 specialized cooperatives in 1980. The average area of state farms increased to 7600 ha and that of cooperatives to 4000 ha [7].

By the end of the 1960s, restrictions on backyard farming had been lifted, made possible by the entry into force of Act III of 1967.

A decision of the Council of Ministers, which came into force in 1975, stipulated not only that the backyard economy should be accepted but also that it should be promoted [8].

Overall, by the early 1970s, small-scale production had become an integral part of agriculture. A division of labor was established in which large farms played a dominant role in the well-mechanized sectors, while small producers played a dominant role in the production of products requiring more manual labor [9].

The new land law adopted in 1987 marked a major turning point in the life of small farmers. It widened the possibilities of acquiring and using land. The old law defined the size of a backyard farm as 800 square hectares. However, the new law also allowed individual farms to use land of other types. The new provision allowed individual ownership of up to 15 ha [10].

The relationship between small farmers and cooperatives has been significantly altered or broken following the change of regime, the compensation process and the transfer of assets [11].

In Hungary, radical changes in economic life took place in the late 1980s and early 1990s, creating the conditions for a market economy.

The effects of this economic transformation did not leave agriculture untouched. As a result of the transformation processes in agriculture, the former farm structure was completely reorganized.

The large-scale reduction of state and cooperative ownership led to the emergence of private property, but after compensation the average size of farms per farm did not reach 1.5 hectares [12].

In the new farm structure that emerged, there appeared dwarf farms with small holdings and economic companies that could only maintain their agricultural activity by renting land. Farmers who became independent were faced with a number of problems which they were unable to solve because of their economic size, and in many cases, they became completely vulnerable to market conditions.

By the mid-1990s, many landowners had abandoned farming, preferring to sell or rent their land. This process has transformed the unity of land ownership and land use, while at the same time, it started a process of concentration, in land use [12].

By the late 1990s, the process of concentration continued. And as the managers of the family farms that emerged after the change of regime moved closer to retirement age, the issue of farm transfer became timely.

For years, professional organizations have been calling for the creation of conditions to support a successful generational transition. As a result, Act No. CXXIII of 2020 on the Family Economy entered into force on 1 January 2021.

2.2 Family Farms Today

On 30th November 2020, the Parliament adopted a bill regarding a comprehensive reform of the family farming system, which came into effect on 1st January 2021.

The law defined the family farm system (Figure 1).

Accordingly, a family farmer is: "...a natural person aged 16 or over who is registered in the register of family farmers and who carries out a family farming activity on his/her own holding." "... may carry out his activity either independently or as a member of a family holding of farmers." (Act CXXIII of 2020, § 3, paragraphs 2-3) [6].

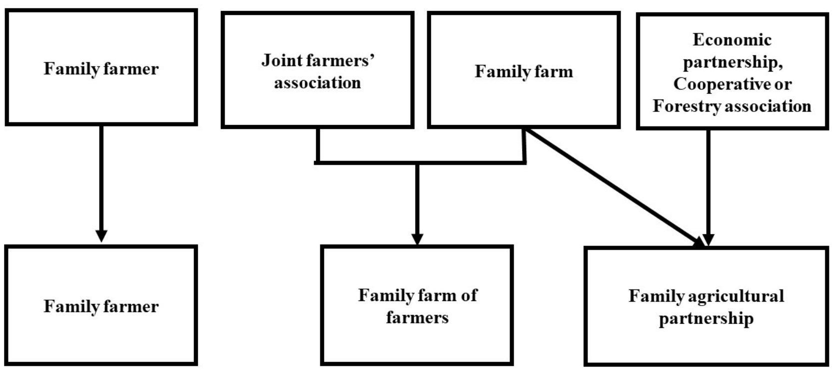

Figure 1
The family economic system in Hungary under Act CXXIII of 2020
Source: [13] based on own editing

The family farm of farmers is defined as "a production community established by at least two members of an agricultural holding who have their own juridic personality and have no separate assets from those of their members. It consists of at least two members of the agricultural holding who are related to each other, within which the agricultural holders carry out their farming activities on their holding jointly, based on the personal contribution of all members in a coordinated manner." (Act CXXIII of 2020, § 6, paragraph 1) [6].

Finally, a family agricultural partnership is considered to be: "... an economic partnership, cooperative or forestry association which is entered into the register of family agricultural partnerships and which is engaged exclusively in agricultural, forestry or complementary activities as defined in the Land Traffic Act, and which has at least two members and who are related to each other." (Act CXXIII of 2020, § 14, paragraph 2) [6].

First, we review what characterizes family farms in Hungary, based on the KSH 2020 agricultural census data [14].

Family farms are predominantly (71%) managed by men. The average age of farm managers is 57.9 years. While in 2010 almost a quarter (28%) of farms were managed by a person aged 65 or over, this proportion increased to 35% by 2020. The 60-69 age group is predominantly responsible for the management of today's farm businesses. (Figure 2)

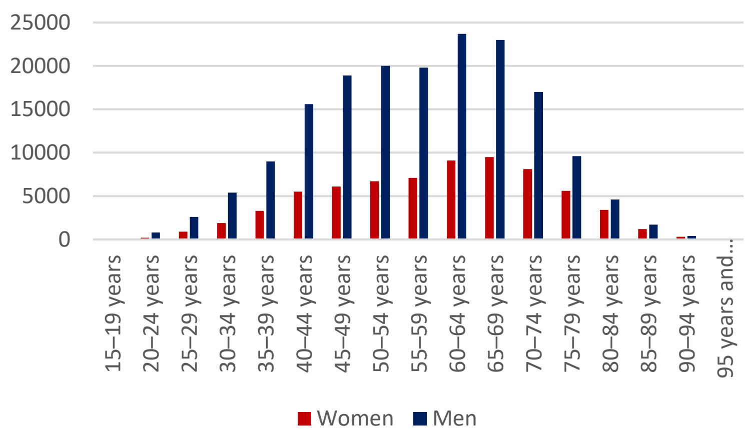

Figure 2
Number of managers of agricultural holdings by gender and life-category in 2020
Source: [14] based on own editing

However, the ratio of managers with an agricultural education has increased: while in 2010 19.8% had either secondary school education or a higher education degree, this rate increased to 38.7% in 2020 (Figure 3).

The survey also gives an idea of how family farm managers envision the future of their farms and that of themselves, and for how many years they plan to farm.

First of all, it is important to note that almost half of the respondents (45%) did not answer this question.

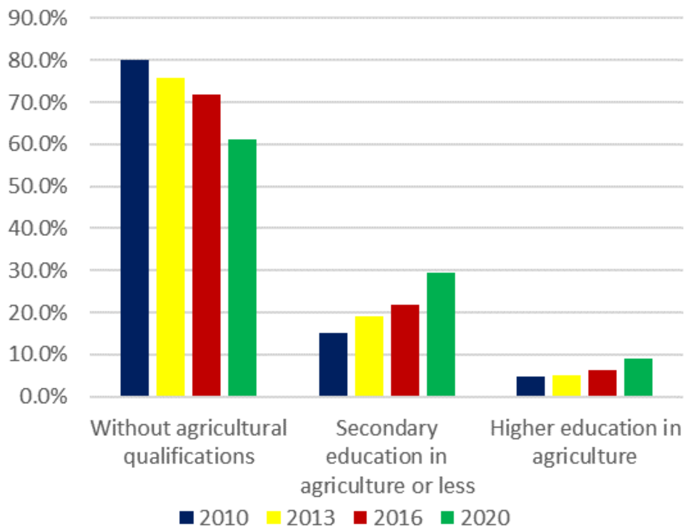

Figure 3
Distribution of the number of holdings by the manager's qualifications
Source: [14] based on own editing

33% of respondents envisage 5 years or less as a farmer, 20% plan to be active for 6-10 years and 47% said they would like to be a farmer even after a decade. It is important to note that the average age of farmers is high (see Figure 2), which may explain the responses.

Data from the 2020 agricultural census also show that 53% of family farm managers consider a maximum of 10 years of active farming, therefore it is crucial to address the issue of generational change [14].

It is also pertinent to look at the data on farmland, which is of crucial importance and can have a significant impact on the costs of farming.

The 2020 agricultural census data show that in Hungary, 216000 farms managed on nearly 4.922 million hectares.

Of this agricultural land, 45% was used by the owners 50% as tenant-occupied 5 percent was used under other claims (sharecropping, land use at farm gate).

Farmers using less than 5 hectares of land mainly cultivated their own land, while the proportion of rented land exceeded 75 percent for those who cultivated more than 300 hectares (Figure 4).

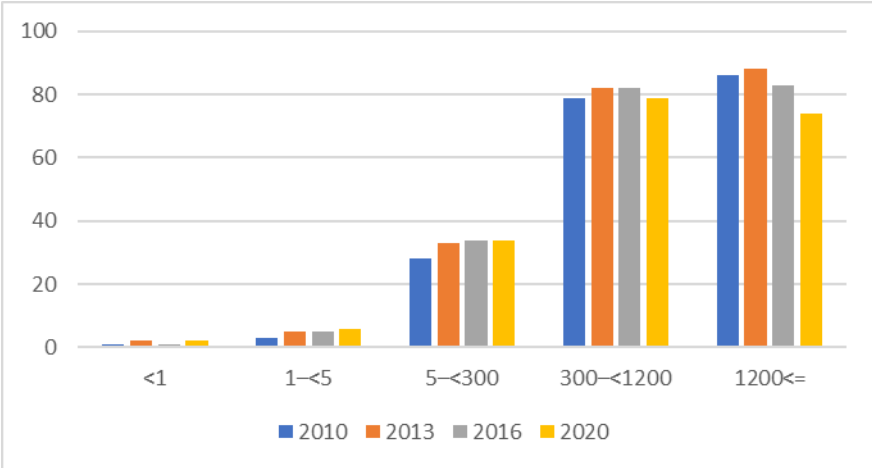

Figure 4
Ratio of rented land by size category (percentage)
Source: [14] based on own editing

Generally speaking, the price of land purchased in 2010 already tripled by 2021. The inflationary environment in 2022 could further stimulate farmland sales, and growing demands can push prices even higher.

The main reasons for the unabated rise in farmland prices over a decade are:

- Higher than average profitability of crop production
- The size of area-based subsidies
- The tax exemption of income derived from the leasing of land for at least five years
- Higher than average crop prices over many years
- A relatively favorable interest rate environment, a stable supply of funds for the purchase of farmland and the continued high level of bank activity in agriculture [15]

The most expensive county is Békés (price per hectare of 2.36 million HUF), Hajdú-Bihar, Pest, Tolna, Fejér and Győr-Moson-Sopron counties also cross the 2-million-HUF threshold (Figure 5).

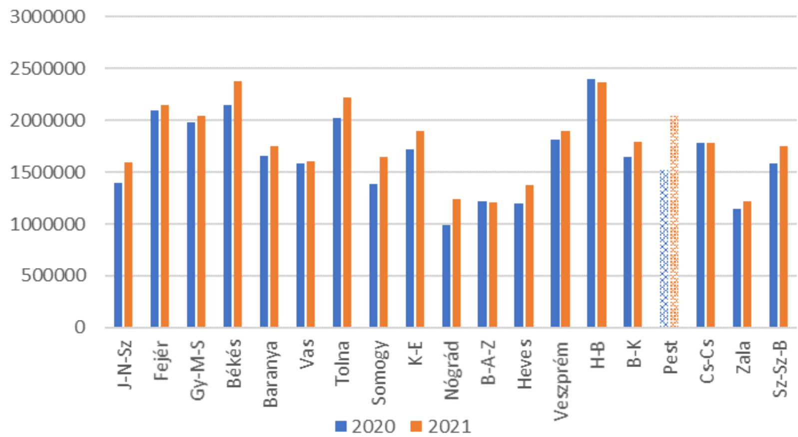

Figure 5

Average farmland prices by county

Note: The price spike in Pest county is due to technical reasons. The processing of the turnover data is significantly behind schedule here, so the column for Pest County in the chart is marked with a line coloring due to uncertainty.

Source: [15] based on own editing

2.3 Future - Tasks to be Accomplished

The ageing of population, declining fertility and expanded educational opportunities for young people challenge the intergenerational sustainability of family farming and present particular difficulties for smallholder farmers. [16]

The nationally less than favorable composition of the agricultural labor force suggests that the nature of the work, being bound to villages, the low dependency and income-generating capacity of the sector are not attractive to young people [17].

This is also supported by research carried out by European Economic and Social Committee (EESC), which found that the low level of income from farming is one of the main holdbacks of attracting young farmers to the sector. The EESC also pointed out that there is a large gap between the income generated by farming and the income available in other sectors of society in rural areas [18].

Research shows that succession decisions are significantly influenced by governmental economic policy, farm assets, age and education of present-day farmers [19].

Other research suggests that young people may be discouraged from farming for the following reasons [20]:

- Economic insecurity, uncertainty and difficulties specific to the agricultural sector

- Rural life is less attractive for young people
- Land prices (Figure 5) and rents are very high compared to incomes
- High initial start-up costs
- Farms cannot be run efficiently without agricultural and business management skills

However, the Common Agricultural Policy (CAP) resources for the period 2023 thru 2027, will be earmarked for young farmers, after Hungary's Strategic Plan for the CAP for the period 2023-2027 was approved by the EC on 7th November 2022. The total budget for the next five years of the domestic CAP is €14.7 billion, of which €8.4 billion will be provided by the European Union for Hungary [21].

From 2023 onwards, an increased focus will be on:

- Support for small and medium-sized farms
- Encouraging generational change in agriculture
- Encouraging the adoption of more environmentally sustainable farming practices (closely linked to this, for example, the extension of the concept of eligible area)

The measures of the CAP Strategic Plan are based on 2 pillars. Pillar I includes direct payments, while Pillar II covers rural development payments (Table 1).

Table 1
Measures of the Common Agricultural Policy Strategic Plan [21]

Direct payments - Pillar I	**Rural development payments – Pillar II**
— Basic Income Support — Redistributive payment — Agro-ecological Program — *Supporting young farmers* — Production coupled subsidy	— Agri-environmental management program — Organic farming — Natura 2000 compensation — Forestry measures — Investments — Cooperation — Risk management — *Supporting young farmers* — Knowledge base and information exchange

As Table 1 shows, both Pillar I and Pillar II, include options to support young farmers.

In order to facilitate generational transition, the CXLIII. Law regarding the Transfer of Agricultural Holdings, which reads as follows in its preamble: "The goal of the Parliament is to facilitate the transfer of farms as unique assets, created by the participation of family members, the joint use of their resources and the results of their work for their common well-being, to the next generation to ensure the efficiency and viability of the economy by preserving the diversity and strengthening the adaptability of agriculture and to help ensure balanced income conditions for the farmers who start, operate and develop farms." [22]

The Act provides for the possibility of transferring farms and all their elements (e.g., land, personal estates, real estates, property rights, etc.) in their entirety.

3 Family Farms in Hungary

Family businesses, including family farms, nowadays have many positive features from an economic point of view, similar to those of SMEs. Many national and international studies [23-33] have examined both SMEs and family businesses.

Among their findings, the following positive characteristics are highlighted:

- Their role in job creation is significant
- They are flexible and can adapt very quickly to constantly changing market conditions
- They are highly motivated
- Adaptable
- Growth-oriented
- Have moderate risk tolerance
- Constantly seeking new opportunities
- They play an increasingly important role in international trade
- Have an active role to meet local needs
- Contribute to the diversification of economic activity and thus to the stimulation of competition
- Play a significant role in employing people with disabilities and disadvantaged workers
- Are innovative and creative
- Are based on strong social networks
- Are based on strong family ties

- Changes in the roles and in the relationships of family members have a clear impact on decisions when setting up a business
- They are long-term thinkers (family heritage and strong personal ties make them want to preserve their businesses for their heirs)
- They have a long-term perspective (they can make appropriate decisions for the long term, even if this means sacrificing short-term income)
- They are stable [28]

As noted above, the generational transition of family businesses in Hungary has already started and is about halfway through, in a very difficult environment: the coronavirus epidemic, the Russian-Ukrainian war and unfavorable macroeconomic environment may significantly set the process of management handover back. Our own research shows that, due to the adverse environmental factors, many members of the successor generation decide to postpone passing the torch and try to navigate their businesses themselves in this chaotic economic and social environment. As one of the family business managers put it, "Now is not the time for the new generation to try to take over. Now is the time for quick decisions and to have leadership experience in order to survive."[1]

So, passing the torch is not a simple one-step process.

This is in line with Ip and Jacobs (2006), who argue that the period of time needed to integrate the successor and achieve full effectiveness is, in their experience, between 12 and 18 months [35].

The same authors have also identified the steps in the process of generational change (Figure 1).

International research also shows that the long-term survival rate of family businesses is low [36]: experience shows that 30 per cent of businesses survive the first generation and 15 per cent the second [37].

The organizational culture and managerial behavior of domestic family businesses are characterized by owner-manager dominance, which makes it difficult to pass the torch. Another typical mistake in generational change may be that personal attachment becomes dominant over competence in the appointment of a successor. Thus, the lack of management competences can jeopardize the long-term survival of the business [38].

[1] Our ongoing research analyzes family farms in terms of genertional change.

Section 1

Assessing the challenges and constraints of succession planning

Psychological and business issues

Legal issues

Financial issues

Tax issues

Section 2

Preparing the succession plan

Background

- Pre-succession company evaluation
- Determination of the predecessor's method of leaving
- Predecessor characteristics

Events

- Leadership development
- Job and staff specification
- Finding a suitable successor

Consequences

- Post-succession performance
- Change in enterprise value
- Management assessment

Section 3

Application of methodologies

Background

- Business valuation
- Determination of exit options
- Engagement and potential successor assessment

Events

- Leadership training
- Job and staff evaluation
- Implementing succession
- 180-360 degree evaluation, feedback
- Benchmarking

Consequences

- Management, job and staff appraisal
- Analysis of business performance and profitability
- Analysis of changes in enterprise value

Successor integration period - 12-18 months to reach full efficiency

Figure 6

Three-stage succession process model [35] based on [26]

In addition to the above factors, other questions about the success of generational change can arise right from the first steps [39] [40], even before the process has started. Here are some of them:

- Does the founder really want to pass on his business to his successors in time or does he wait too long until the suitable successor has already chosen his or her own occupation? When is the optimal time to hand the management of the business over? There is no universal answer to this question. However, the research work of Handler provides some guidance in the context of succession. [39] It shows that there may be a positive correlation between the level of education of the successor, his/her work experience outside the company and the success of the generational change. In addition, it is important to gradually involve the successor in the business. Here, it is essential that the manager in office works side by side with the successor, involving him or her in the business and handling responsibility, authority and leadership gradually over. To do this, however, it is essential that there is a successor within the family who can (is capable) and wants to take the business over.
- If there are several suitable successors within the family (e.g., siblings) who could and want to take the torch over, the question may arise: how can rivalry between siblings, for example, be resolved? Ward makes the following suggestion [41]:
    - In successful family businesses, both siblings and the parent-owner work to ensure that sibling rivalry has a positive rather than a negative effect.
    - They can use techniques such as:
        - Defining a general and well-publicized philosophy for regulating salaries and promotions
        - Designating separate positions for siblings within the company
        - The development of a code of conduct to regulate the behavior of siblings towards each other
- If there is an offspring within the family who may be suitable to take the business over, but whose age or inexperience, for instance, does not make them suitable, it is possible to appoint an interim manager with the help of a consultant until the offspring is ready.
- If there is no lineal successor within the family who is able or willing to take the family business over, there is still the option of appointing a professional manager (with appropriate control but retaining ownership).
- If none of the above options are available to the family, the business may be sold or, ultimately, liquidated [42-44].

Conclusions

The role of family farms is significant in Hungary. Therefore, it is of utmost importance that the process of generational change ahead of them, goes smoothly. There is currently no tradition for farm transfer in Hungary and the transfer of the family farm management is hampered, by a number of factors.

The number of older people in the Hungarian agriculture is significantly higher than that of young people, thus, the number of young people entering the sector cannot replace the number of older people leaving it, as is also the case in many European countries. The lack of adequate replacement strategies can threaten the long-term survival of farms in Hungary.

Arable land plays an extremely important role in the life of farms. The price of farmland has already tripled, on average over a decade. By 2022 a high inflationary environment, boosted farmland sales even further, with demand growth driving prices even higher.

Land is a scarce resource. For the long-term survival of family farms, it is essential that land owned and used by the farm, remains in single ownership and is not fragmented.

In recent times, a number of measures, laws and support schemes have contributed to the success of this process, aimed at generational change and the efficient operation of family farms.

The targeted support of the Common Agricultural Policy's, Strategic Plan for the period 2023-2027 or the Act CXLIII of 2021, can further enhance the smooth and successful generation change and the unification of land ownership for the family farms in Hungary.

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