

DIVESTMENTS IN THE PROCESS OF DEVELOPING OFF-FARM ECONOMIC ACTIVITY BY FARMERS¹

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Abstract. The purpose of this paper was to initiate discussion of the role of divestments in transformation of farms which diversify their activities towards off-farm economic activities. This paper is theoretical, supplemented with results of surveys conducted among farmers-entrepreneurs. Observations and studies of literature references indicate that in course of development by a farmer of off-farm economic activities, available farm resources are involved first. After a certain time, considering significant disproportionality in economic efficiency of resources involved in competing activities, and in view of difficulties in obtaining new resources from outside, a need arises for divestment within the farm. Typically, this leads to decreased significance or even marginalization or abandonment of the less profitable activity, which is typically the farming activity.

Key words: divestments, farm, economic activity

INTRODUCTION

In the concept of multifunctional rural development, actions improving the ability of farmers' families to earn additional income are strongly emphasized, which can be achieved, among other ways, through taking up jobs by persons simultaneously involved in agricultural activities, so-called pluriactivity [Wilkin 2009, Krakowiak-Bal 2010]. At the same time, both in subject-matter literature [Kaleta 2005, Klepacki 2005, Kropsz 2009] and in economic practice [Program... 2011], farm diversification is mentioned among the possible earning alternatives by farmers' families. Government documents strongly emphasize the need to diversify the activities of residents of rural areas towards off-farm activity. According to Bład [2008], diversification should be treated as a nar-

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rower concept than pluriactivity: "...most researchers agree that diversification applies to activities taken up on a farm or depending on the farm, based on land and capital resources. In this meaning, diversification can be perceived as a sub-group of the broader term pluriactivity, comprising all forms of generating incomes from non-agricultural activities, whether on or off-farm".

The key factor which determines whether a farmer's additional economic activity should be considered pluriactivity or farm diversification shall be the definition of the strength of relationship between the economic activities and farming activities. If non-agricultural economic activity carried out by landowner is functionally related to the agricultural activity (without agricultural activity, non-agricultural activity would be prevented or significantly hindered) or if there is a socio-cultural relationship between these activities (e.g. agritourism, handicrafts, crafts), then this would be a form of diversification of farm activities. On the other hand, if there is no functional relationship between the agricultural and non-agricultural activities, then it should be perceived as pluriactivity while the farm and the non-agricultural undertaking should be considered two separate entities, related by equity.

Commencement and conducting of economic activities requires involvement of labour and capital resources, often as well as land. Resources of households are a natural source of these inputs. It is common knowledge that commencement and carrying out of non-agricultural economic activities by a farmer is a good way to manage labour surplus on the farm. It also contributes to involvement of fixed assets for the purposes of non-agricultural activities, thus leading to increase and improvement of their utilization.

Increasing demand for capital during the process of business development, with limited options of obtaining funds from outside, also triggers the need for divestments, which are defined in subject-matter literature as: "...voluntary (scheduled) or enforced by a crisis (temporary) limitation of previous scope (profile) and scale of operations of an undertaking and discontinuation (withdrawal, liquidation) or disposal (mainly through sale) of certain activities" [Lovejoy 1971, Osbert-Pociecha 1998]. Funds gained from sales of the farm's assets and equity items and labour moved through reallocation can be used in newly formed or developed non-agricultural economic activities.

The primary objective of this paper was to initiate discussion of the role of divestments in transformation of farms which diversify their activities towards off-farm economic activities. Theoretical part was supplemented with available numerical data concerning scale and extent of non-agricultural economic activities carried out by families operating farms in Poland. In view of the lack of current data, the authors used data for individual farms which were engaged in agricultural activity in 2007 [GUS 2008]. To illustrate the impact of non-agricultural activities on the scale of agricultural activities, the authors used the results of a survey conducted among a group of 159 business operators from the following poviats: Dąbrowa, Kraków, Jasło, Ropczyce-Sędziszów, who were insured with the Farmers' Social Security Fund in 2011.

A FARM AS A POTENTIAL AREA FOR DIVESTMENT

Research by the Central Statistical Office showed that in 2007, 2,387.2 thousand of all the 2,575.1 thousand individual farms (92.7%) were engaged in agricultural activities

in the territory of Poland. The following tendencies continued to be observed [Frenkel 2009]:

- lowering number of individual farms,
- lowering number of farms engaged in agricultural activities,
- lowering number of smallest farms, up to 5 ha in size, with simultaneous growth of the number of larger farms, beyond 20 ha of cultivated area,
- lowering number of persons employed at farm,
- increasing number of persons combining work on farm and off-farm,
- increasing level of formal education of individual farm operators,
- increasing percentage of farms earning incomes from employment, non-agricultural economic activities, old age and disability pensions, and other non-work sources,
- decreasing percentage of households for which agricultural activity was the main source of income and of farms earning incomes mainly from non-work sources,
- increasing percentage of farms earning incomes mainly from employment and farms earning incomes mainly from non-agricultural economic activities.

Of all the farms engaged in economic activities in 2007, almost 114 thousand (ca. 4.8%) were simultaneously engaged in agricultural and non-agricultural activities². The prevailing category comprised activities related functionally to the agricultural activity (Table 1). Of those farms which were simultaneously engaged in agricultural and non-agricultural activities, there was a significant group of farms using their own equipment in service activities (28.5%); moreover, a significant percentage of farms were engaged in agritourism and letting rooms (8.9%) as well as plant cultivation and breeding animals in aquatic environment (9.9%). The less frequent activities included: wood processing (5.9%), processing of agricultural produce (2.6%), crafts (1.8%), and production of renewable energy for the market. A very large group comprised activities classified as other (45.7%), but their functional relationships with the agricultural activity would usually be significantly lower. Activities consisting of energy production from renewable sources would mainly be carried out at the largest farms, while the popularity of economic activities consisting of wood processing was similar in all farm size classes. Interest in earning incomes from crafts would decrease in proportion to increase of farm size, which can be explained by lesser available labour resources with increased scale of the farm's agricultural production. In other types of studied non-agricultural economic activities, higher frequency of occurrence of non-agricultural activities was observed with increase of farm sizes. For operators of smaller farms, employment outside the farm would be a more typical way to seek extra income. Similar conclusions were reached by Paszkowski [2007] in his research, who also pointed out that farms exceeding 50 ha in size would more often combine their agricultural activity with off-farm economic activities. He also mentions that farms with scarce resources of land would more often abandon their agricultural activities and focus on non-agricultural activities only.

²To reach the full number of farms pursuing non-agricultural economic activities, the above specified value should be summed up with farms pursuing exclusively non-agricultural activities. In 2002, according to PSR, there were approximately 103 thousand farms engaged in non-agricultural activities only.

Table 1. The share of farms conducting non-agricultural economic activity in the number of farms pursuing agricultural activity depending on the scope of activity and farm area (2007)

Tabela 1. Udział gospodarstw prowadzących pozarolniczą działalność gospodarczą wśród gospodarstw prowadzących działalność rolniczą w zależności od zakresu działalności i powierzchni gospodarstwa (2007 rok)

Farms conducting economic activity in the field of:	Farm area groups in ha					
	0–1	1–5	5–10	10–20	20–50	> 50
	the share of farms pursuing activity different than agricultural					
– providing services using own equipment	0.8	1.4	1.6	1.7	2.0	4.1
– agritourism, room rent	0.3	0.4	0.4	0.5	0.8	1.3
– processing of agricultural products	0.0	0.1	0.2	0.2	0.3	1.0
– wood processing	0.3	0.3	0.3	0.3	0.2	0.4
– handicraft	0.1	0.1	0.1	0.1	0.1	0.0
– aquaculture ^a	0.3	0.3	0.5	1.0	1.8	2.6
– production of renewable energy for the market	0.0	0.0	0.0	0.0	0.0	0.1
– other ^b	2.0	2.4	2.1	1.9	2.1	3.9
Total	3.8	5.0	5.2	5.5	7.3	13.3

^aPlant cultivation and animal breeding in water environment.

^bIncluding fur animal husbandry.

Source: Author's own elaboration on the basis of: Charakterystyka... [GUS 2008].

Źródło: Opracowanie własne na podstawie: Charakterystyka... [GUS 2008].

Data of the Central Statistical Office indicates that the number of farmers deciding to take up non-agricultural economic activities was the highest in the following voivodeships: Małopolskie, Mazowieckie and Łódzkie [GUS... 2008]. This data is not entirely credible, considering the varying areas of these regions and varying number of farms operated in these regions. The highest percentage of farms pursuing non-agricultural activities was in voivodeships with relatively larger farm sizes, i.e. Zachodniopomorskie, Łódzkie and Warmińsko-Mazurskie. Farmers' proactive attitude in taking up non-agricultural economic activities, characteristics and scale of these activities are determined by multiple factors. Apart from location and farm area, other prevailing factors are: individual capabilities of the farmer's family members, their ability and readiness to take a risk [Basaj and Kotala 2009, Zajac 2010].

DIVESTMENTS VS. NON-AGRICULTURAL ECONOMIC ACTIVITIES

Diversification of activity of an undertaking may take place on the basis of external or own resources. Large entities with highly valuable assets are more easily capable of obtaining an investment credit. Small farms typically seek the opportunity to finance new activities on the basis of their own funds or EU aids. The Rural Area Development Programme for 2007–2013 envisages an option to obtain funds directly for diversification of farm activities, under axis 3 measures: "Diversification towards non-agricultural activity. Formation and development of micro-enterprises. Nevertheless, involvement of own resources remains the issue of key importance. The need to make divestments would

occur very frequently: “Divestments in a farm shall mean scheduled and conscious limitation of agricultural production and/or involvement of a farmer’s household resources in agricultural production activities, leading to release of certain land, labour and capital resources which can be used in other agricultural or non-agricultural activities, consequently leading to an increase of the farmer’s and his family’s income” [Wojewodziec 2010]. Increase of personal income³ may be caused by increase of agricultural income, reduction of farm losses or reallocation of resources from less economically efficient activities to the more efficient ones, e.g. from agricultural to non-agricultural activity, or taking up off-farm employment in lieu of labour-consuming agricultural activity.

The following activities should be considered divestments in family-owned farms:

- with regard to production: extensification, limitation or abandonment of production, giving up of selected production activities,
- with regard to land management: renting, fallowing, exclusion from agricultural use in favour of development, afforestation, sale,
- with regard to capital management: change of utilization pattern of the farm’s fixed assets (e.g. using them for purposes of non-agricultural economic activities or for family support), sale⁴ or alienation of fixed assets,
- with regard to labour resources management; commencement of non-agricultural economic activities or taking up off-farm employment by persons working on farm [Wojewodziec 2010],
- with regard to organization: split of farm.

Decker and van der Valden [2006], within their resource-based approach, distinguish between two basic forms of disinvestment: repositioning and reconcentration. Repositioning involves a change of primary activity while reconcentration consists of abandonment of peripheral activities in favour of the primary activity.

Repositioning may occur through evolution or revolution. Evolution is typical of activities that are functionally related to the prior basic activity. New activities initially occur as supplementary activities. Only with market development, acquisition of new technologies will it become possible to pursue repositioning. A revolutionary change of primary activity would mainly occur in the event of shareholding changes in an undertaking. However, it may also occur as a consequence of bold decisions, adapting the undertaking’s activities to changes in turbulent environment.

Similarly, reconcentration may occur slowly or rapidly but it will always ultimately lead to higher specialization of production. It may involve abandonment of production in supplementary activities with simultaneously retaining their potential in the corporate structure (in case of farming, this may be for instance fallowing of land), or division and splitting of secondary operations from the undertaking (sale, outsourcing).

A family-owned farm is an economic entity which combines the qualities of an undertaking and a household. A farmer’s household and production farm jointly establish a family farm with a joint budget of the two component parts. A household offers inputs to the production undertaking and obtains incomes in exchange, i.e. remuneration for work,

³Personal income is the sum of incomes from a farm and incomes generated from off-farm activities.

⁴Referred to as disinvestments in related literature, e.g. Osbert-Pociecha [1998].

profit, and possibly landowners' pension. The process of creating a small non-agricultural undertaking on the basis of a farm can be divided into three major stages:

- initiation of non-agricultural economic activity,
- reallocation of the farm's resources to non-agricultural economic activities (repositioning),
- abandonment of the agricultural activity and development of non-agricultural activity (reconcentration).

In the first stage, new use is sought for available farm resources. Farm diversification towards non-agricultural activities, or commencement by a farmer of economic activities that are not functionally related to the farm will very soon exhaust the farm's available resources. Further development of non-agricultural activities requires engagement of extra resources, having their sources outside the farm (such as credit, employees) or inside the farm (e.g. divestments).

With restricted ability to obtain outside resources, the farmer is encouraged to reallocate, move his resources from these activities where they are less efficiently utilized to those where they would generate higher incomes. The flow direction is typically a movement of resources from agricultural to non-agricultural activities. Thus, divestments take place, consisting of gradually depriving the farm of its labour and capital resources. Farm production shrinkage with simultaneous growth of non-agricultural production leads to a change of primary activity, or repositioning.

The consequence of continuation of this process will be reconcentration – limitation of all activities only to the non-agricultural business. A family farm will be transformed into a household with an owner of land and a non-agricultural undertaking. Household resources will be used by non-agricultural business (undertaking) while farmland will be leased, rented, afforested, or left idle.

The dynamic process of development of a non-agricultural undertaking on the basis of a farm's resources could be considered a process of "creative destruction", through which existing activities are cannibalized by the new business initiative.

From the viewpoint of corporate theory [Osbert-Pociecha 1998], the described process of formation of a non-agricultural entity on the basis of a farmers' family resources should be considered an anticipating divestment, a part of restructuring of that business entity. Giving up one type of operations (farming) gives an opportunity for development of another type (off-farm activity). Divestments in the farm, which take place in this situation, constitute one of the elements of the process of its transformation into a non-agricultural establishment. In terms of agricultural economics, the farmer's business initiative should be perceived as formation of a new economic entity which is not a part of the existing farm. The farm has then the common owner with the newly formed undertaking, the undertaking uses the farm's input resources, and palliative divestments can be observed within the farm itself, often leading to its liquidation.

If farm land remains with the business operator as a consequence of the above described process, and the operator himself earns high profits from his business activities, he may return to agricultural activities in the future. However, it is highly probable that such activity will be pursued as a hobby or sentimental activity. Farming should be perceived among receding industries.

A survey carried out in 2011 among entrepreneurs insured by the Farmers' Social Security Fund showed that the scale of farming activity of persons engaged in non-agricultural economic activities is very small in the vast majority of cases. For over 40% of surveyed farms the population of livestock would not exceed 0.1 LSU while crop production was limited only to production for own purposes (Table 2). In the remaining group of farms, the most typical behaviour was stabilization of production on a very low level. The average number of animals in this group was 0.36 LSU per farm, and the area of 2/3 of all farms would not exceed 5 ha. It should be pointed out at the same time that the vast majority of farmers taking up non-agricultural economic activities were not engaged in agricultural activities at the time of taking up the former, while owning land only gave them access to the cheaper social security system for farmers.

Table 2. Structure of farms by changes in agricultural production
Tabela 2. Struktura gospodarstw według zmian w produkcji rolniczej

Year of commencement of non-agricultural activity by farmer	Number of farms in group	Without agricultural production in 2012	Changes in the respondent's farm production during the last 5 years		
			increase	stable	decrease
percentage of farms					
2010–2012	17	52.9	5.9	41.2	0.0
2005–2009	39	35.9	10.3	41.0	12.8
2000–2004	50	52.0	6.0	36.0	6.0
1995–1999	30	36.7	3.3	43.3	16.7
Before 1995	23	26.1	17.4	43.5	13.0
Total	159	41.5	8.2	40.3	10.1

^aFarms in which the number of animals does not exceed 0.1 LSU and crop production is generated for self-supply only.

Source: Own research.

Źródło: Badanie własne.

SUMMARY

In course of development by a farmer of off-farm economic activities, available farm resources are involved first. After a certain time, considering significant disproportionality in economic efficiency of resources involved in competing activities, and in view of difficulties in obtaining new resources from outside, a need arises for divestment within the farm. As a consequence of development of the more efficient activity, the less efficient operations are cannibalized, which are most commonly the agricultural activities. This process takes place in three phases. In the first phase, non-agricultural economic activity is initiated; the second phase is repositioning (replacement of primary activity from agricultural to non-agricultural); in the third phase, reconcentration occurs (abandonment of supplementary activities, including agricultural activity).

The process of repositioning a farm's production activity need not necessarily lead to ultimate discontinuation of agricultural activity. However, statistical data indicates that there is a vast number of farms engaged only in non-agricultural economic activities

(over 100 thousand). At the same time, commencement of non-agricultural business can be more and more frequently observed among land owners who have discontinued their agricultural activities and for whom a significant reason to show entrepreneurial behaviours is the preference social security system for farmers.

Both endo- and exogenous factors determine the character, extent and rate of divestment in a farm simultaneously pursuing non-agricultural activities. The impact of functional relations between the various activities, their profitability, economic potential of the farm, availability of investment resources, etc. on the rate and direction of change must be verified. To identify them and determine their strength, in-depth empirical research would be necessary.

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DYWESTYCJE W PROCESIE ROZWIJANIA POZAROLNICZEJ DZIAŁALNOŚCI GOSPODARCZEJ PRZEZ ROLNIKÓW

Streszczenie. Celem opracowania było zainicjowanie rozważań nad rolą dywestycji w transformacji gospodarstw rolniczych dywersyfikujących swoją działalność w kierunku pozarolniczej działalności gospodarczej. Opracowanie ma charakter teoretyczny uzupełniony wynikami badań ankietowych przeprowadzonych wśród rolników-przedsiębiorców. Przeprowadzone obserwacje i studia literatury wskazują, że w trakcie rozwijania pozarolniczej działalności gospodarczej przez rolnika w pierwszej kolejności angażowane są wolne zasoby gospodarstwa rolnego. Z czasem jednak, przy dużych dysproporcjach w efektywności ekonomicznej wykorzystywania zasobów zaangażowanych w konkurujących ze sobą działalnościami oraz wobec trudności w pozyskaniu nowych zasobów z zewnątrz, następuje potrzeba dokonania dywestycji w obrębie gospodarstwa. Zwykle prowadzi to do zmniejszenia znaczenia, a nawet marginalizacji lub zaniechania działalności mniej opłacalnej, a tą na ogół jest działalność rolnicza.

Słowa kluczowe: dywestycje, gospodarstwo rolne, działalność gospodarcza

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