

ICPS newsletter

Ukrainian agriculture needs comprehensive government policy

Agriculture accounts for a significant share of Ukraine's GDP; it also plays an important social function, since the rural population almost entirely depends on it. However, despite its huge potential, the sector continues to suffer from inefficiency and non-competitiveness. These two factors point directly to the urgent need for reform in Ukraine's agriculture.

Reforms in the sector have been sluggish, and major problems still remain unresolved. While the problems are numerous and their nature is not unique to Ukraine, some of them need to be addressed first in order to ensure the success of the whole reform process. Crucial areas where urgent improvement is needed include state policy development and implementation, farm restructuring and land reform, and rural financing.

These problems are discussed in the latest issue of ICPS's Policy Studies publication. The editors of this issue of Policy Studies are Frank Bostyn (frank.bostyn@ua.ac.be)—Director of the MBA program at the University of Antwerp Management School (UAMS); and Andriy Boytsun (andriy.boytsun@ua.ac.be)—a doctoral student and research assistant at the University of Antwerp. Both editors had long experience of work with the Permanent Secretariat of the Inter-Ministerial Commission for Agricultural Reform (now known as the Secretariat of the Presidential Commission on Agricultural Policy) in Ukraine

In Ukraine, agriculture represents almost 18% of GDP and even a greater share of country's total employment. It has an important social function, since the rural population (which makes up approximately 30% of Ukraine's total population) almost entirely depends on it. Furthermore, the performance of Ukraine's overall economy is largely dependent on the fortunes in the agricultural sector; and the GDP fall in recent years has been largely due to the decline in this sector. The contribution of agriculture to export revenues is in line with its part in the GDP.

Despite the strengths of Ukrainian agriculture, its output has been falling in the past decade. In 1999, Ukraine's agriculture shrank to less than a half of its 1990 size. The decline has been due to both overall economic factors and to the lack of any new industry-specific policy (for many years agriculture remained the least reformed sector in Ukraine's economy).

Hence, improvement in the rural economy is very much contingent on the success of agricultural reform, which must eventually lead to an effective agricultural sector. It is extremely important to secure the sustainable

profitability of this sector, given its share in Ukraine's GDP.

Agricultural strategy outline

Success of agricultural reform is mainly determined by government ability to develop and implement a sound reform strategy. Still, many problems remain in this area, among which the most important are:

1. Inadequate capability to analyse policy requirements.
2. Lack of co-ordinated policy formulation and implementation.
3. Inadequate administrative structures.
4. The influence of those having a stake in halfway reforms.
5. The influence of conservative forces.

The potentials of agriculture and the rural sector in general might be very important; however, the right economic and institutional conditions are not really in place to let them fully develop. Ill-conceived agricultural policies account for a large part of the decline in Ukrainian agricultural output.

Preconditions for an effective reform strategy

In order to succeed with reforms, the administrative structure of the agencies

responsible for implementation of the government policy in the sector should be tackled right away and in a radical way. However, the functional reorientation of the ministry should not be seen as an isolated act, but should be incorporated in a global strategy for developing effective governance structures in Ukraine, adapted to a market economy, that would be instrumental and not obstructive to the policy set by democratically elected bodies.

Building blocks for an agricultural strategy

This strategy, as a conceptual plan with a broad and detailed action scheme, should emerge from the Ukrainian policy formulation process itself, and should not be "imported" by granting one or another blueprint by outside advisers the status of an official plan by decree. That way, it will simply not work.

Elements of the reform strategy should be carefully elaborated, taking into account their costs, effectiveness and implementability, the risks of effective obstruction and misuse of policy measures for group interests, proper timing, co-ordination and consistency of the measures, etc. In other words, the

process should be driven by realism and pragmatism.

To be successful, the plan must be broadly accepted by and committed to by the administrative/governance structures which have to implement it. This means that it is imperative to engage these structures already at the formative stage.

Taking into account the very nature of sectoral reform strategy in a transition economy, the basic philosophy of it should be as follows: the overall objective is to increase the wealth of the nation and its population in a sustainable way. Therefore, it is necessary to improve the economic efficiency of the sector. The right way to do this in a market economy is to create the proper general environment that can induce increased efficiency at the microeconomic (enterprise) level. Hence, the government should aim at ensuring:

- a proper macroeconomic and legal environment;
- effective markets; and
- further enterprise restructuring.

Farm restructuring and land reform in Ukraine

Due to the distribution of land shares and privatisation of the land previously used by collective agricultural enterprises, one specific level where significant changes are being observed is that of leasing relations. Land leasing has two different connotations in Ukraine. In addition to conventional leasing, which implies transfer of use rights to a specific plot of land for a specific term, leasing may also involve transfer of land shares from individual shareholders to farm enterprises or other individuals. Currently this is the dominant form of land leasing in Ukraine, although the practice of leasing physical plots is growing. At the same time, buying and selling of farmland is virtually nonexistent in Ukraine, primarily because of the continuing legal moratorium on such transactions.

There is considerable diversity among the restructured farm enterprises in Ukraine, and where a new generation of

Ukrainian sugar: Developing an industry restructuring policy plan

The Ukrainian sugar industry has declined sharply over the last decade. In general, the industry cannot withstand competition in the world market, both in terms of quality and price, and hence, the whole sector needs redressing. From an economic point of view, the straightforward answer would be to discontinue growing sugar beets altogether; however, at social and political level, the immediate social fall-out in terms of layoffs looms large. Pressure from within is high to keep sectors artificially going with heavy state intervention and subsidisation, but that kind of solution is not sustainable in the long term. Nevertheless, the government has continued to apply mainly ad hoc measures to artificially support the sector, while a long-term strategy is still missing. A successful long-term strategy should include measures aimed at ensuring efficiency at both macro- and micro-economic levels, while also addressing social problems.

farm managers has come in, there are often innovative approaches to internal organisation and operations management. On the whole, however, the farm restructuring efforts so far have failed to radically change the entrenched collective organisation of Ukrainian farms.

Policy measures for agricultural recovery

While farm restructuring generally has the potential for improving productivity and efficiency of agriculture, the accomplishments in Ukraine have been very modest. The major reason for this is that the overall economic and policy environment has not improved—and so, quite to the contrary, it has remained the major impediment to creating market-based agricultural enterprises.

Prospects for the revival of Ukrainian agriculture will largely be determined by the government's willingness to adopt a number of basic policy measures, aimed at:

- relaxation of inflexible bureaucratic procedures inherited from the command-administrative regime;
- development of competitive factor markets;
- liberalisation of external trade;
- effective restructuring of farm enterprises;
- development of alternative employment opportunities in rural areas to allow shedding of agricultural labour as a prerequisite for productivity improvement;
- speedy resolution of the impasse in the maintenance and development of

rural social infrastructure, through allocation of necessary budgets to local governments.

Financing problems in Ukrainian agriculture

In Ukraine, agricultural enterprises depend almost exclusively on short-term external capital, while the share of bank credits in external financing is constantly shrinking. Input suppliers and the state remain the major lenders to agricultural enterprises. As of the end of 1999, the total debt of Ukrainian agricultural enterprises exceeded 15 billion hryvnias (around \$3bn). While the debt burden is rather low by international standards, indebtedness remains a severe problem due to the low profitability of farms.

Agricultural enterprises are not able to attract needed external financing due to their low profitability, high production risks, lack of creditworthiness, significant transaction costs, and lack of collateral. However, the problem is aggravated by the weakness of the banking sector in Ukraine. In addition, the necessary institutions (including efficient bankruptcy and banking laws, bookkeeping systems, and the credit registry) are not in place. Consequently, in order to overcome financial problems in agriculture, Ukrainian government policy should address all these concerns. ■

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