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Ukraine

Agricultural Situation

Slow Pace of Reform

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Report Highlights: Agriculture in Ukraine, which should be the source of wealth, generating tax revenue, exports and lucrative employment, is instead in a catastrophic state. Most farms are heavily in debt, the provision of inputs is steadily declining and agricultural production is dropping to drastically low levels. Increasing state interference, antiquated regulations and bureaucratic procedures are major barriers to the development of powerful private markets for agricultural inputs and outputs.

Includes PSD changes: No
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Agricultural reform in Ukraine has been slow and uncertain. The more dramatic progress made during the initial years following independence in 1991 in land privatization, open markets for the supply of inputs and farm commodities, private ownership and operation of land and agricultural industries has slowed significantly. Since the 1996 drought, a vicious circle has developed. Government provision of agricultural inputs, and subsequent farm debts to the government, have led the state to continue to assert control over crop output, thereby reducing the availability of commodities that can be sold to pay off debts to private sector farm input-providers. Positive fundamental changes are now expected to come more slowly than had been anticipated earlier by the international community.

What Has Been Achieved

Until mid-1996, the near inability of the Government of Ukraine (GOU) to effectively intervene in agriculture, and some positive steps to support private farmers, seemed to auger well for future rapid reform. Between 1992 and 1995 the number of private farmers expanded from less than 2,000 to 35,000 under a program supported by the GOU. (This is in addition to the estimated 15.6 million private plot and subsidiary plot holders from which family needs and increasing overall production are being realized.) Private independent commodity exchanges were trading substantial quantities of commodities. Private U.S. agribusiness partnerships were rapidly expanding the provision of farming inputs, processing facilities and marketing outlets.

The expectation was that the private sector would expand to serve some 25 percent of the total farm area within three or four years. While private land ownership was clearly a difficult policy issue, there seemed to be widespread, grass roots support for large farm restructuring and issuance of land titles. Collective and state farm workers were provided certificates of land share. Industry workers were provided shares in the ownership of commodity-handling and food-processing facilities.

Prices were generally liberalized and many internal price controls were discontinued. Domestic prices for products more closely reflected world commodity prices. Direct and indirect subsidies to the agriculture sector were sharply reduced or eliminated, due in large part to GOU budgetary constraints. State control of agriculture was significantly weakened. Farm managers for the first time were able to make significant production and marketing decisions. In addition, foreign and domestic trade was substantially liberalized. Domestic producers for the first time were forced to compete with imports.

What Has Not Changed

By mid-1996, however, a number of adversities overtook Ukrainian agriculture, and a different set of approaches to solving the problems of agriculture began to emerge. This began with the drought in 1996, which seemed to provide the rationale for the GOU to restrict private grain movements in order to reserve as much grain as possible for the Government. This immediately reduced private sector access to grains produced on the farm, disrupted operations of the commodity exchanges and private input supply, processing and marketing enterprises. Open market commodity trading dropped sharply, and private input supply companies, foreign and Ukrainian, could not collect on their contracts.

While farm and factory workers were given shares in land and factories, the management and operation of the collective farms and processing industries changed little except in name -- from kolkhoz to collective agricultural enterprise (CAE) and joint-stock companies. Most of these farms and factories continued to be run as the personal fiefdoms of the farm and factory directors.

Unfortunately, efforts of farm directors to manage more independently and to make more market-oriented decisions were devastated by Government intervention and confiscation of crops from the still mostly state operated marketing and transportation channels. Since 1996 more and more farms became insolvent; thus today over 90 percent of the collectives are bankrupt and on average repay only one-third of all loans received. The GOU in August 1996 created Khlib Ukrainy (Bread of Ukraine) which has operated as the new government monopoly controlling the grain market. Other programs were initiated by the GOU to supply inputs, fertilizer and machinery, which in turn, were supported by Khlib Ukrainy collection of grain from the farm for payment.

Support for private farmers within the GOU and the Parliament also slowed. Few new private farms have emerged since 1995 and the environment they face has deteriorated. Tax requirements have become complicated and burdensome.

Despite some hard-earned GOU support (as a potential source of farming inputs) and continued progress in large farm restructuring and land titling under a USAID sponsored project, opposition to private land ownership remains strong and vocal in the Parliament and in many parts of the Government. Some of the opposition comes from directors and bureaucrats who fear a loss of control. But there also exists the fear that private land ownership will some how allow for foreign domination of the countryside and a feudal future for the rural populace, as financially pressured small land owners sell out cheaply to foreign corporations.

Consequences of the Halt in Reform

A practical consequence is that farms cannot offer land – their most valuable asset -- as collateral for loans. The produce of these farms remains the only possession of any marketable value and, consequently, the target of state and commercial exploitation. This lack of collateral creates conditions wherein only the state provides credit, and only in the form of barter inputs. In return, the state claims first right to all commodities produced on the farm.

The GOU rationale for its significantly more active participation in agriculture seems to be the following:
A) Land privatization will be a slow process given the high level of political opposition; B) Existing farms are bankrupt and, therefore, cannot be made commercially viable through private sector efforts; and C) Private sector institutions (credit, support services, legislation, real estate laws and markets) are inadequate to support private agriculture or agro-industries which do not yet exist in Ukraine. Thus, for the moment, large-scale land leasing seems to be the chosen solution to collateralize land for purposes of realizing a source of inputs, and in the process to prevent the breakup of the large collective farms.

Based on the above chicken-and-egg rationale, the GOU maintains that the state must continue to support agriculture through supplying inputs and must, in return, receive crops as repayment since the farms lack cash or access to credit. But the dismal financial situation of the farms has led supporting fertilizer and fuel industries to export increasing quantities of their production rather than making it available to unprofitable local agricultural producers. GOU and Parliamentary rhetoric that this practice should be stopped has had little effect thus far.

Serious reservations exist among the present generation of leaders about abandoning the structures and processes of the past and promoting the process of market reform and private enterprise in general, especially in agriculture. Clear evidence of this orientation to state control was GOU willingness during 1996-97 to extend sovereign guarantees for the purchase of large-scale agricultural equipment, which can only be used on the collective and state farms, in spite of farm indebtedness and lack of farm repayment potential. Control over the distribution of agricultural commodities is a major source of revenue for government entities, a source which they are reluctant to surrender.

Future of Agriculture in Ukraine

A renewed government focus on agriculture was evident in the appointment this spring of a Vice Prime Minister to address policy reforms in agriculture. Thus far the Presidential Commission on Agrarian Policy has adopted only a decision stating that further reforms in land will be based on land-leasing. The Commission's conclusion was that it was too early to talk about full privatization of land. The leasing law is seen as a transition until the time when land will be made a marketable commodity. Thus far only some five percent of arable land is under rental agreements. This will increase as Government authorities see this avenue as a source of bringing farming inputs to the debt-ridden farms.

Meanwhile the number of individual land shareholders willing to break away from their mother farms is extremely low. Private farms will not increase in the short run since the only land available to them is poor, sandy or marshy lands. Private farmers are mostly deprived of the opportunity to rent land since most collectives have yet to demarcate allocated land shares.

Likewise, while the first step has been made in privatizing the national network of grain receiving stations and elevators, this privatization effort has yet to afford the measure of security on the control of grain and oilseed shipments necessary for the survival of the private sector.

Unfortunately, Ukraine is not realizing the benefits which agriculture is capable of contributing to the growth of the overall economy. Increasingly stringent GOU budget constraints have meant less than necessary inputs being supplied to agriculture. An increasing area of excellent arable land is not being farmed. Crop and livestock outputs continue to decline. The positive balance of trade in agricultural commodities, which in 1996 was 1.6 billion dollars, was only 224 million dollars in 1998.

Ukrainians, meanwhile, are not going hungry. Sufficient food exists for survival of the people, thanks to the 15.6 million village/city garden and plot holders whose production of vegetables, fruits, berries and livestock products has been steadily increasing. But with fewer commodities available for domestic processing, unemployment becomes greater and the risk of social disruption increases.

Hopefully the state will see the need to mobilize its resources to resolve the important tasks of establishing contractual law, an effective court system and ensure the rule of law. Perhaps then the spread of land ownership, even considering current restrictive ownership rights, will eventually generate the momentum for increased land privatization and realization of a land market. But, at present, it is difficult to be optimistic about the near-term prospects of Ukraine's agriculture sector.