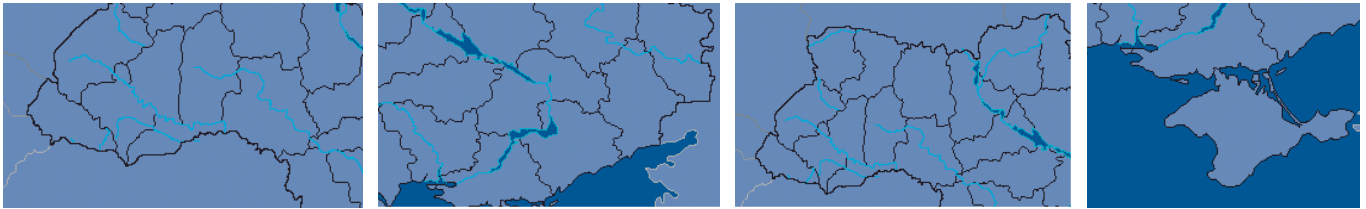




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Putting Agricultural Competitiveness and Rural Well-Being On an Equal Footing Long Term Strategies for Rural Ukraine

■ In order to leave the remaining legacies of the Soviet system behind, the rural area in Ukraine needs to be re-defined as an attractive place of living and not only in terms of agricultural production.

■ Agricultural development is often addressed separately from other policy sectors. The impact of the economic and food crises has however shown that new integrated policy strategies must tackle poverty in general and aim at sustainable livelihoods for the (rural) population.

■ The Ukrainian agricultural sector is also in the need of reform and especially lacks medium sized farms. With stable framework conditions leading to predictable effects on individual farmers, incentive structures for new agricultural undertakings are created.

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Introduction

In times of economic difficulties, policies often focus on urban centres with the aim to support industrial development. As a result, more and more especially young people move to the cities and contribute to rural depopulation and aging. This also applies to Ukraine and stands partly in contrast to the Ukrainian officials' deep conviction of the great potentials of the agricultural sector. The increasing number of individual decisions to migrate from the countryside has however not led to the implementation of a comprehensive rural development strategy. Taking into consideration the close interrelation between rural and urban development, such a policy is however indispensable for Ukraine as a whole and crucial for the effective assessment of transition decisions.

The Ukrainian rural population finds itself in the midst of an ongoing transformation process. Due to the policymakers' focus on agricultural development, policies to ensure social well-being on the countryside are largely absent. Especially during the first decade after the breakup of the Soviet Union, rural poverty was on the increase and drove more and more people into subsistence agriculture. Moreover, the agricultural structure and quality standards do not conform to those in the European Union (EU) so that further European integration requires substantial reforms.

This paper seeks to explore the opportunities for rural development in Ukraine and particularly assesses the role that agriculture can play therein. In a first part, the state of Ukrainian agriculture and rural development is set in perspective of the historical legacies from Soviet times. Second, policy options as part of a long term strategy for Ukrainian rural development are suggested. Special emphasis is in this connection put on the integration into the European agricultural space. In conclusion, a summary of the findings leads over to a future outlook.

Cultivating New Farms: Building Upon Soviet Inheritance

Equipped with its rich black soils, Ukraine was one of the bread baskets of the Soviet Union. However, despite its own large natural resources, the USSR needed to import grains because Stalin's enforced collectivization resulted in many years of unproductive collective farming and famine. Irresponsible agricultural production methods limited the country's production possibilities: Excessive strain and incorrect tillage of the former kolkhoz (collective farms) led to soil erosion and steppe-forming. Additionally, agricultural and rural development were closely interwoven. The rural life was structured around the kolkhoz which assumed all socioeconomic functions. It can therefore be stated that the Ukrainian agriculture today has to struggle with the legacies of half a century of mismanagement. Still in 1998, the part of unprofitable companies among the Ukrainian agricultural producers amounted to 92% (Lerman et al, 2007, p.19).

During the 1990s, the situation of Ukraine did not improve despite her independence from the Soviet Union. The downfall of the kolkhoz, rural flight and a massive lack of capital contributed to reduced grain production. Continued government intervention in the form of quotas on agricultural exports, grain procurement, reluctance to liberalize trade¹ and further state support for large farms aggravated the situation (pp.15-16). Many rural residents were driven into subsistence farming during this period, perceived as temporary solution to the worsening trends in food availability and affordability. For the population left on the countryside, the agricultural companies still performed important socioeconomic functions. As „the farm enterprise took over the functions normally fulfilled by local government“ during Soviet times (p. 78) this could not change overnight. Since 2000, however,

1 Features of a closed economy could be observed on different levels. Whereas the central government maintained minimum export prices, local authorities prohibited sales to other Ukrainian regions in order to meet the region's quota.

this role of the local farm has been transforming²; Even though the corporate farms still assist private farming undertakings, these services are now financed by those who are benefitting (pp.3-5).

Privatization of agricultural land was a lengthy process in Ukraine. After paper land shares had been handed to the rural population in the early 1990s, nothing changed substantively until December 1999 when a presidential decree commanded their conversion into fully titled land plots for the shareowners. In this way, seven million Ukrainians were allocated physical land³. The landowners needed to agree for a corporate farm to be able to use the land any longer. Nevertheless, a moratorium interdicts the selling of land (p.1). The resulting replacement of the farms based on collective land ownership by family farms, private enterprises, farming corporations and agricultural cooperatives altered the agricultural statistics overnight. Caution is needed when considering statistics of this time as many old collective farms only changed their corporate form. Up to today today, many agroholdings and large farming enterprises are operating in Ukraine.

The reform in 1999 has however led to important results. Whereas 95% of agricultural land had been under control of collective farms before 1990, this part has shrunk below 60%. At the same time, individual farms (new private farms and household plots) not only increased their share in total but also their particular size. Combined with the number of unprofitable farms declining significantly, the individual farms contributed largely to the agricultural recovery: a growth of 30% between 1999 and 2004 (p.2). Nevertheless, the Soviet dual farm structure is still present. This manifests itself in the corporate farms being

considerably larger than those of the private sector. A household plot in Ukraine is almost 12 times smaller than the average in the EU-15 (p.3). Consequently, a lack of productive mid-sized farms can be noticed.

Designing Appropriate Policies

The development of the rural area including the agricultural sector is determined by initial conditions, natural resources and policies. Ukraine is endowed with a very diversely structured agricultural sector with differing soils and diversified production possibilities. With a mixed-forest zone in the West (production of potatoes, flax, vegetables), the rich black soil to the South East (spring wheat, barley) and a veld further to the South East (black coal sources), areas for agricultural use are available nearly all over the country. However, agricultural policies also need to acknowledge for this high heterogeneity of the rural areas.

It is often stated that the agricultural output of Ukraine can be tripled once the country attracts enough investments. However, the question arises in how far productivity growth contributes to sustainable rural development: How can agricultural progress be combined with assured rural livelihoods? Policies need to entail measures that enable all producers to benefit, f.i. from price increases through a proper market infrastructure. Any long term strategy should thus seek to render the transition to a market economy socially as just and reasonable as possible.

Strengthening Non-Agricultural Markets

First and foremost, rural residents must be given the opportunity to decide on their own whether to seek employment in the agricultural sector or not. The availability of off-farm employment prevents them from facing only the choice between going into subsistence agriculture or to migrate from the countryside. Also the modernization of agriculture needs to be accompanied by the development of industrial, commercial and service sectors (processing,

2 This transformation set in considerably slow due to the reluctance of the central Ukrainian government to allocate the needed budgets to the local councils which were supposed to take over the social services functions.

3 Rural individuals today own 70% of agricultural land.

agroindustry, commercial and transportation infrastructure). More non farm employment in the rural area can then provide employment possibilities for the newly unemployed due to technical progress towards more capital intensive farming. The trend of declining rural populations but constant shares of employed in agriculture (Lerman, 2007, p. 8) does not seem to be sustainable. In this sense, off-farm employment contributes to the raising of rural incomes. Agricultural producers in Ukraine (both corporate and private farms) mainly focus on primary agriculture within the boundaries of the farm gate so that high potentials emerge in the development of nonagricultural activities. In the private sector, processing is moreover not yet widespread. The willingness to engage in new activities can be initiated by courses of instruction for private farmers in order to enable them to engage in more capital-intensive production methods.

The strengthening of nonagricultural markets on the Ukrainian countryside however presupposes skilled entrepreneurs and workers whose education needs to be secured. The possibility to make a living in rural environments also helps to slow down the urbanization process in Ukraine and the accompanying problems arising in overpopulated cities⁴. Moreover, the improvement of education can be seen as strategy to combat the lack of efficiency in the Ukrainian agricultural sector. This lack is combined with labor supply difficulties resulting from the absence of skilled workers, the decreasing number of young workers⁵, decreasing motivation and „bad habits“ like alcoholism and unreliability (Lerman et al., 2007, p.8). Future policies

need to focus especially on the attraction of young persons to the rural areas. In order to create an incentive structure, not only attractive employment opportunities and schools but also leisure facilities like sports clubs should be available.

Agriculture as Part of a Rural Development Strategy

Although off-farm employment constitutes one major part of a strategy for the rural future, the importance of a new view on agriculture may not be neglected. Rendering farming attractive however remains a difficult task and can only be achieved if just conditions apply. It can in this regard be recommended to mainstream the social insurance system. Many household plot farmers whose monthly income is above the minimum wage face the difficulty of not being able to pay to social insurance because a large part of the income taken into account is not available in cash but in home-grown and consumed products. This course of action further impoverishes the rural residents due to their lack of old age security (Lerman et al., 2007, p.26). As long as rural poverty is not fought resolutely, nostalgia may remain popular among the population. Although one can objectively note that the Soviet way of farming was not efficient, for most rural people the end of collective farming did not bring substantial improvements. This sensitivity towards the past needs to be both understood and overcome. Although from an economic viewpoint, an agriculture in small scales may not be necessary, consultation and support for small-scale farmers can increase the life quality of the rural population which, in the end, should not only depend on the mechanisms of the free market.

The continuation of the reform of the land market is another important policy measure. If private farmers can attain more land, their commercialization will increase with the plot size (p.6) and more mid-sized farms will help Ukraine adjust to the international agricultural standards. The securing of transferability of land will reduce the fragmentation of the Ukrainian land structure.

4 The rural population in 2005 accounted for 80% in relation to figures from 1980.(Lerman, 2007, p. 8)

5 A survey conducted by Lerman et al (2007) revealed that 50% of the respondents (rural Ukrainians) prefer their children to leave the villages. This figure is confirmed by the evidence that only 24% of the farmers and 8% of the total rural population regard agriculture as future career for their descendants.

The overall aim needs to be the development of a sustainable agriculture. This also includes the cautious treatment of natural resources and thus total abandonment of harms like incorrect ways of irrigation and drainage which lead to pollutant mobilization. The possibilities for the moderation of climate change should be taken into account in all policy decisions. Moreover, quality is one of the main criteria for competitiveness on the European market and its attainment can be facilitated with the introduction of slower and greener farming methods. The state can support this development with targeted subventions. Ukraine thus faces the decision whether it wants to produce at low costs and quality or embark on a strategy of product diversification.

Reforming the Role of the State

Above all, a paradigm change away from the belief in large corporate farms and the associated economies of scale towards trust in the peasant farms which in fact are not less productive than their large counterparts is necessary (Lerman et al., 2007, p. 9). Mid-sized farms dominate in most market economies and agricultural policies need to live up to the needs of these new farms by way of a total retreat from interference at the farm level. Instead, the focus needs to lie on the completion of framework requirements. In this regard, a clear strategy is needed so that its effects on individual farms are clear and predictable. This also means that in order to combat inequality, no longer most government support policies may focus on large farms but they must aim at establishing equal chances for all corporations (Galushko & Cramon-Tudell, 2004, p.226).

New policies need to focus on breaking the path dependency inspired by the Soviet system and stable framework conditions are a prerequisite for the trust in all reform policies. In this regard, measures which do not interfere with market mechanisms can be recommended in case they also do not require transfers from the consumers but can be financed by public sources. These can include individual long

term support programs for particular farms or the improvement of the market infrastructure (producer communities, roads, water ways, regular and transparent reports on prices and markets). Additionally, research, consultation and education can support the consolidation of the reforms. In order to make producers sensitive to cautious working, grants for insurances against production risks can help in the same way as rewards for environmentally friendly production. In order to raise quality standards, the introduction of process oriented veterinary and phyto sanitary standards is necessary (Lissitsa & Strubenhoff, 2005, pp.10-11).

The rural inhabitant needs to be the focus of any policy. Due to the important role that farming still assumes for the Ukrainian rural population, sustainable rural development means both the securing of agreeable conditions for agricultural producers and the buildup of an infrastructure encouraging a new generation to stay on the countryside and take part in the transformation of rural life in Ukraine. In order to meet the expectations of the younger generation, their inclusion in decision making processes needs to be guaranteed.

Integration in the European Agricultural Space

The EU has defined the „European Model of Agriculture“ in terms of a combination of international competitiveness with high product standards and rural well-being. Agricultural activity is supposed to not only „produce food but also to guarantee the survival of the rural area as a place to live and work“ (Petrick & Weingarten, 2004, p. 2). This EU policy is however not directly responsive to the needs of the countries in Central and Eastern Europe where agriculture often represents a poverty alleviation strategy and a development strategy for agriculture is needed most (p. 3).

Since the enlargement in 2004, Ukraine has become a direct neighbor of the EU. The EU-Ukraine Action Plan stipulates that „the pace of progress of the relationship will acknowledge fully

Ukraine's efforts and concrete achievements in meeting commitments inclusion of environmental concerns in inter alia regional development and agriculture and asks for the adoption of the new land code which also enables foreigners to attain Ukrainian land.

Already today, a close association between Ukraine and the EU exists. Ukraine trades most of its agricultural produce with the EU and not anymore with Russia. Whereas Ukraine mainly exports commodities and intermediate products, it imports final products from the EU (European Commission, 2009). For the EU, an even closer association in the agricultural sphere might be especially interesting in light of the scarcity of animal feed. However, EU quality standards still differ from those in Ukraine.

The approximation to and integration in the EU's Common Agricultural Policy will

and common values". Concerning rural development, the Action Plan calls for the most probably remain one of the most contested issues during any future EU membership negotiations. In its efforts to further European integration, Ukraine can draw on the experience of the enlargement procedures in 2004 and 2007. Especially Poland has had a similar initial position. This means that the country should embark on a reform course before membership negotiations start. As stated in the first two parts of this paper, Ukraine still faces many challenges and also rates comparatively weak in relation to the other Central European states, especially when considering its advantageous soils (see figure below). Once reforms have led to results in the first requested target areas, Ukraine can consider to ask for support programs like SAPARD or LEADER+.

Selected comparative economic indicators for Ukraine and the new EU members

	Ukraine	Hungary	Czech Rep.	Slovak Rep.	Poland
GDP per capita, 2004 (US\$ at PPP)	6,317	16,639	19,381	14,519	12,881
Agriculture value added per worker, 2003 (2000 US\$)	1,400	3,991	4,444	n.a.	1,397
Cereal yield, average 2001-03 (tons/ha)	2,4	4,0	4,3	3,8	n.a.
Sun flower seed yield, average, 2001-03 (tons/ha)	1,2	1,8	2,2	2,0	n.a.
Rural population (% of total, 2003)	33	34	26	42	38
Food exports (% of merchandise exports, 2002)	13	7	3	4	8
Employment in Agriculture (% of total, 2001)	20	6	5	7	19
Agriculture value added (% of GDP, 2002)	15	4	4	4	3

Source: Lerman et al., 2007, p.37

Although also Poland had been assessed as slow reformer, it was still seen as much more reform-oriented than Ukraine. The seemingly unwilling reforms until 2000 contributed to a sharp decline and very slow recovery of Ukrainian agriculture (Lerman et al, 2007, p. 41).

Like the WTO accession, further European integration will lead Ukraine towards more open trade policies. However, those will not only have positive results. Farmers and workers in industries which are expected to contract over the years to come will suffer from the developments and it is for these people that rural development strategies need to focus on off-farm employment. At the same time, the Ukrainian state needs to be aware of the arising interest of foreign investors. Foreign investments need to be coupled with clear conditions in order to ensure positive results for both contract partners.

Conclusion

Ukrainian rural development has taken on new forms since 2000. Set in a European comparative perspective, it needs however to be acknowledged that up to today, large parts of the Ukrainian agriculture are organized according to the Soviet model, with many small farms sharing a tiny proportion of the total agricultural land and few large farms having the control over an area that is proportionally out of scale⁶.

In light of the economic crisis and the large part of their budget that households allocate to food in Ukraine, it becomes clear that agriculture may not be regarded in complete separation from other policy sectors. Food price inflation can not be tackled at the rural development level only; Ukraine needs new integrated policies which aim at an overall sustainable development. Rural development and agriculture constitute a part of this strategy, not more and not less. This also means that supporting rural development can not be measured by the budget allocated to the field. By contrast, it is

mostly the countries allocating few resources to their agricultures whose support is organized most effectively. Although the changeover to a new agricultural and rural development policy may be costly at the start, it will strengthen the sector due to the development towards competitive structures in the long run. Price political measures on the contrary further slow down the structural adjustment processes and make the producers dependent on subventions.

In order to stop the marginalization of rural areas, research on agricultural development should be encouraged. Rural development can no longer be equated with agricultural development but rather represents a continuum to the urban space. When this understanding is established among the population, rural livelihoods may be more attractive for the younger generation as well. Although more professional working methods are welcome, Ukrainian policy makers should not grant them access at any price and be cautious towards foreign 'land grabbers'. Foreign investment thus needs to be reflected critically.

The prevailing lack of competitiveness in the agricultural sector can also be understood in an optimistic way, namely as starting point for growth and hope in the international food crisis. Often described as possibly being one of the rising stars of Eastern Europe, Ukraine should take the initiative itself and play on its potential.

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