

Features of the agricultural subsidies in Ukraine

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This note describes the existing in the country system of the agricultural subsidies and provides with a historical overview of subsidizing Ukrainian agricultural sector.

Introduction

According to the developed by OECD System of National Accounts Methodology¹ subsidies are defined as “grants, which state and private enterprises receive from the government and which represent additions to the receipts of producers of goods and services over and above what they receive from the sales of their output”. These grants do not constitute a part of the market value of the output. However, they can offset a part of the production costs.

In general terms agricultural subsidies are those subsidies, which are provided by the country's government to:

- agricultural loss-making producers for social or other reasons, even if they have little to do with producers' prices;
- specific agricultural products that are paid for each unit of good or service produced;
- use of inputs (i.e., fuel, equipment, irrigation).

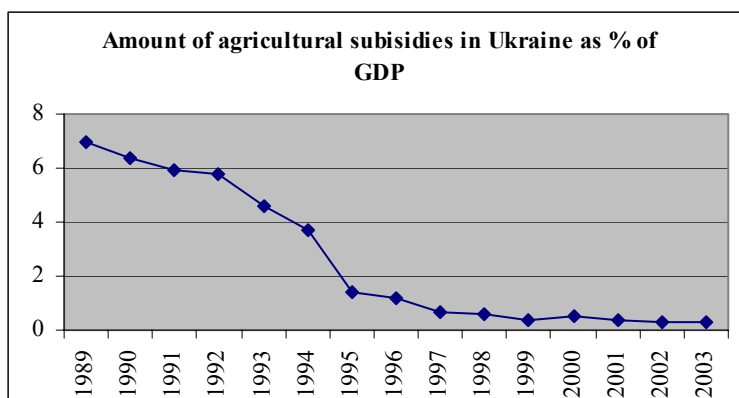
Subsidies to the economy continue to be one of the major items of government expenditures in many transition economies and in Ukraine, particularly. However, it needs to be admitted that agricultural subsidies are used in market economies as well. Subsidies to agriculture, which are essentially price subsidies, are also common in many industrialized and developing economies. At the same time, the majority of such subsidies in developed countries are transparent and ruled by the existing agreements of country and WTO. The situation with subsidies in Ukrainian agriculture is an important component, which needs to be discussed during the country's accession to WTO.

1. Historical overview of agricultural subsidies in Ukraine

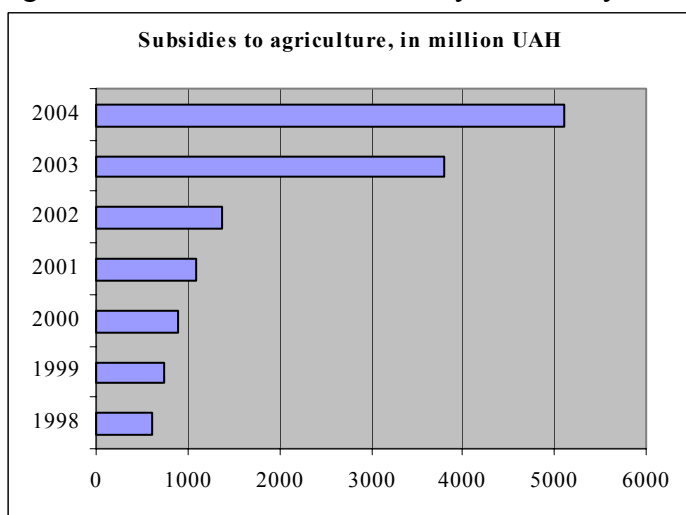
The Ukrainian agriculture still remains one of the major recipients of the government subsidies. The expenditures for agriculture increased within the consolidated budget, while the share of expenditures for industry and energy decreased.

The livestock expansion policy led to increasing agricultural subsidies. By 1989, total subsidies in Ukraine amounted to 13.5% of GDP, of which subsidies to agriculture accounted for 7% of GDP. Since earlier 90-th Ukraine has continued to subsidize its agricultural sector, although the amount of such subsidies decreased dramatically and its annual average did not exceed 5%.

¹ OECD, 1997



Although there was a significant decrease in the related size of subsidies as a percentage of the country's GDP, over the same period of time we can observe an increase of the absolute value of subsidies. They increased from UAH 607.6 million in 1998 to UAH 5,100 million in 2004.² This increase reflects the existing inefficiency of the Ukrainian budget over the studied period of time. The main feature of the budget was a high level of the fiscal deficit. Mainly this deficit was due to the high level of subsidies to the country's economy and to its agriculture, in particular.



However, the amount of agricultural subsidies to the Ukrainian producers (i.e., farmers) was rather virtual than the real one. These were not transfers of the financial assets from the state budget to budgets of the producers. Although the state budget has been fixing the certain funds to be transferred as an agricultural subsidy it was almost never transferred to the final recipients (i.e., agricultural products producers) in a full amount.

Final recipients of the agricultural subsidies were able to receive only a certain proportion of the planned amount of subsidy. According to the data of the Ukrainian State Statistical Committee in 2001-2003 the average annual arrears on agricultural

² We are not able to review the statistical data on amount of subsidies in absolute term before 1998 since these data are not comparable. The main reason for that is the different exchange rate, which existed in the country before the 1998-year-crisis. We are not converting data into the stable currencies because this converting will cause other problems related to the purchasing power and the ratio in agricultural domestic and world prices.

subsidies accounted some 36% of the planned amount of subsidy.³ This reflects (i) the low level of fiscal discipline, which has been existing in the country and (ii) lack of financial resources, which government was planning to spend for subsidies.

In order to increase efficiency within the agricultural sector of Ukraine and, in particular, to put in order all issues related to subsidies for this sector the Law "On encouraging agricultural development in 2001-2004", 2001 was introduced by the Ukrainian Parliament. This Law envisages introduction of supportive prices for agricultural products and presumes income support to the producers through state subsidies. The law sets privileged loans to agriculture and at least a 5% limit for the state allocations to be spent on this sector of the national economy.

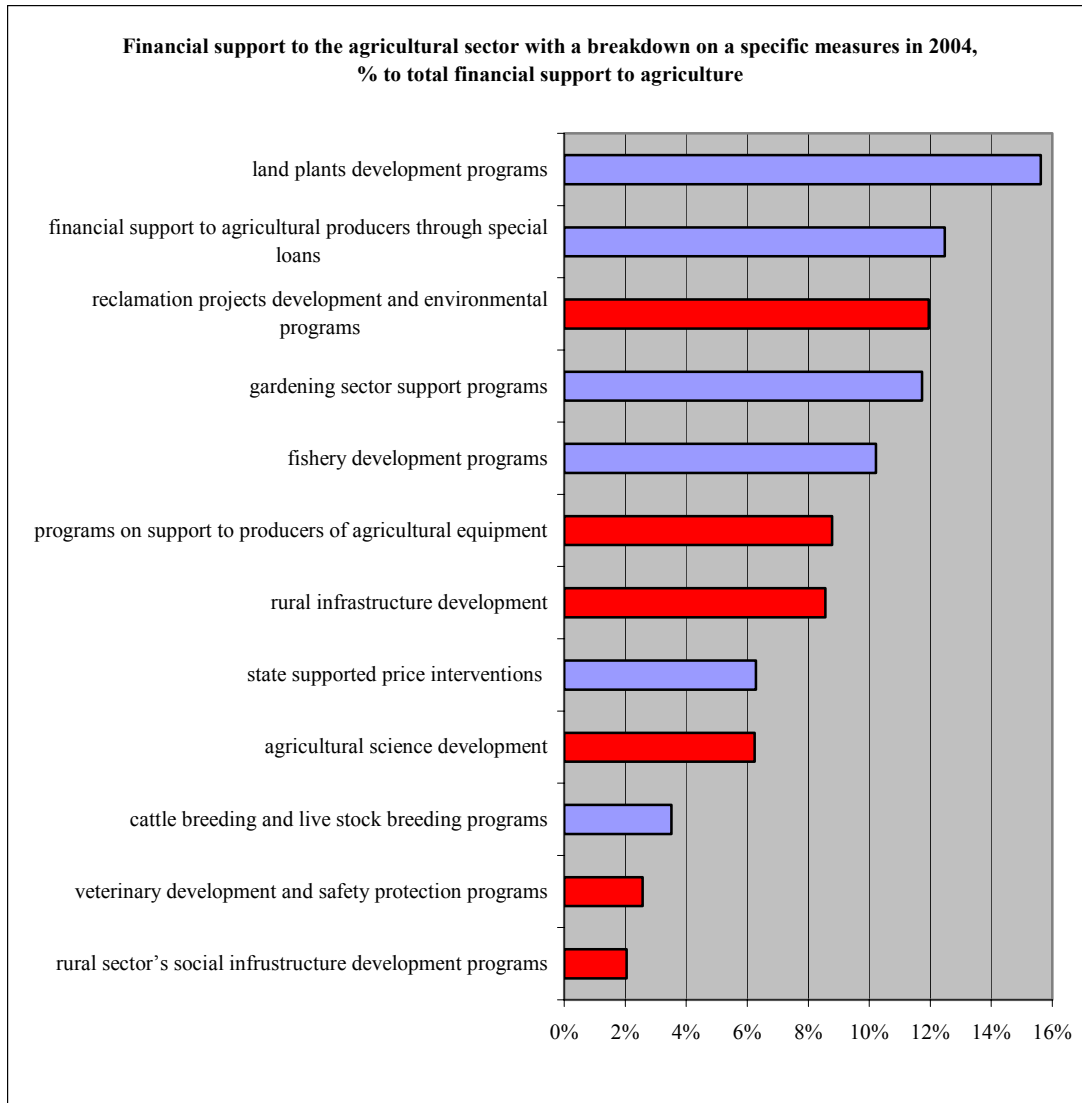
2. Types of the state support to the Ukrainian agriculture

The Ukrainian government provides financial support to the agriculture in a form of direct subsidizing to this sector and in a form of indirect subsidies. According to the existing in Ukraine practice the country's government provides its support to the agricultural producers in different forms. The main forms of the state support to agriculture come as a state financing of:

- land plants development programs
- cattle breeding and live stock breeding programs
- fishery development programs
- reclamation projects development and environmental programs
- financial support to agricultural producers through special loans
- gardening sector support programs
- veterinary development and safety protection programs
- agricultural science development
- rural infrastructure development
- rural sector's social infrastructure development programs
- programs on support to producers of agricultural equipment.

Clearly, not all types of the support provided by the Ukrainian government can be considered as a support to the agricultural producers. It is very obvious that many of those traditional items, which are included into the list of the supporting measures, cannot be considered as agricultural subsidies. For example, rural infrastructure and social development programs as well as agricultural science development programs cannot be considered as those agricultural subsidies, which are needed to be agreed under the WTO rules. However, other subsidies can be the subject of such agreement. In any case, it's crucially important to know the existing in Ukraine structure of state financial support to the agricultural sector with a breakdown on specific measures, in which this support is directed.

³ State Statistical Committee. Data based on '1B Form'. Average overdue payable is presented cumulatively as the end of the each year.



The highest weight in the total structure of the state support to agricultural sector has land plants development programs, which obtains 16% in the total amount of support. Those items, which are not subjects to the WTO regulations (i) reclamation projects development and environmental programs – 12%; (ii) programs on support to producers of agricultural equipment – 9%; (iii) rural infrastructure development – 9%; (iv) agricultural science development – 6%; (v) veterinary development and safety protection programs – 3%; (vi) rural sector's social infrastructure development programs – 2%. All in total the non-related to WTO restrictions items accounts to some 41% of the total amount of subsidies coming to the Ukrainian agriculture. As on the state of 2004 the absolute amount of money, which was transferred for these six items accounts to around UAH 2 billion (USD 394 million), while the rest of the items, which can be considered as related to the WTO agreement items, was UAH 3.1 billion (USD 584 million).

2.1. Land plants and gardens development programs

This type of support to the Ukrainian agriculture has been stable over the last three years and did not exceed UAH 50 million.

Traditionally, over the last decade the share of these two sectors in the total amount of the state financing to agricultural sector has been varying between 20% and 35%. It means that both these sectors have the highest weight in terms of the budget expenditures.

2.2. Cattle breeding and live stock breeding programs and fishery development programs

The 2004 budget reserves UAH 52.7 million for Ukrainian fishery industry support. However, not this entire amount of financing is directed to fishery production per se. Around 20% of this amount was spent to support the work of the shipyards. Therefore, the real amount spent for Ukrainian fishery in 2004 was around UAH 40 million.

In 2004 the Ukrainian cattle breeding and live stock breeding programs received UAH 574.1 million, which demonstrates almost 90% rate of growth compare with the previous year and 15 times more compare with a level of 2002.

2.3. Reclamation projects development and environmental programs

Reclamation projects are an important element for the effective development of the country's agriculture. Traditionally these projects received a significant portion of the state support. For example, around 20% of that support, which was devoted to the Ukrainian agriculture came to the reclamation projects. However, in the middle 90th the support shranked and came down to the current level of 12% in the total structure of the agricultural financing. In 2004 the amount of money spent on these projects was around UAH 384.7 million against UAH 299.8 million in 2003 and UAH 233.4 in 2002.

2.4. Financial support to agricultural producers through special loans

This is a relatively new program, which proves its very low level of efficiency. It made very clear after the collapse of the leading agricultural bank called "Ukraine". However, if in 2002 the weight of these costs in the total amount of the costs were 5% in 2003 they almost doubled and reached 12% of the total amount.

2.5. Agricultural science development

In 2003 the Ukrainian budget expenditures spent for the development of agricultural studies accounts at some UAH 120 million. This money traditionally spends for R&D in agriculture and partly for education of the students in universities with the agricultural profile.

2.6. Rural infrastructure development and rural area social infrastructure development programs

Rural areas in Ukraine are traditionally underdeveloped. Due to this fact this one of the priorities in the Ukrainian policy related to the agricultural sector is to secure support to the rural areas. However, this financing cannot be considered as a subsidy, which is needed to be negotiated during the process of the country's accession to WTO.

Conclusions

1. The Ukrainian agriculture obtained a significant portion of the state budget.
2. Although the financing to the agricultural sector is expanding over the time, the amount of subsidies as a share of the country's GDP has been constantly going down over the last decade.
3. The total amount of the state financing into Ukrainian agriculture in 2004 budget was fixed on a level of UAH 5.1 billion (USD 957 million).
4. The analysis of the existing in the country types of the state support to the Ukrainian agriculture suggests that only 59% of them can be considered as those which are needed to be agreed during the process of negotiations on country's accession to WTO.
5. Although there exists a possibility that Ukraine will be increasing its subsidizing to agriculture it could not be significantly higher than the existing numbers in a hard currency terms.