

# Doing Agribusiness in Ukraine



2011

# Doing Agribusiness in Ukraine

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**Dear readers,**

Agricultural sector of Ukraine is truly an economic backbone and a social cornerstone. Agrarian policy in most countries have already overgrown very narrow framework of simple improvement of profitability of agricultural producers and nowadays it is touching upon issues of sustainable development, preservation of land and water resources, availability and affordability of food and rural development.

A similar process is taking place in Ukraine. Growth of cereal prices shall be taken in view of the necessity to secure stable supply of food at affordable prices;

and such an attitude is justified in the country being a net-exporter of food.

Efforts of the Government aiming at establishment of farmland market are accompanied with development of legislation providing for a duty of land users to care for preservation of fertility of soils, as soon as Ukraine is called upon to ensure food supply for many generations of Ukrainians as well as for people of other countries.

Investment attractiveness may not be supported solely by low ground rent or weak social responsibility of business, because any investments need certain living environment to unfold in.

There is an ongoing search for compromises and win-win solutions building upon due account of social and economic interests existing in agro-industrial complex. Sometimes this search is taking a bumpy road, and some decisions are criticized in the sector, but we are confident that solutions found decades ago do not match the challenges brought about by post-crisis economic environment.

On behalf of the Ministry of Agrarian Policy and Food of Ukraine I assure you that our search for new solutions for persisting and new problems in the field of agriculture and food will be focusing on attaining of our primary goal, well-balanced improvement of investment attractiveness of Ukraine.

I do hope that readers of this brochure will be able not only to benefit from ongoing reforms, but also to make their contributions into release of agrarian potential of Ukraine!

Minister of Agrarian Policy  
and Food of Ukraine  
Mykola Prysyzhnyuk

A handwritten signature in blue ink, which appears to be 'Mykola Prysyzhnyuk'. The signature is fluid and cursive, written on a white background.

**Dear colleagues!**

You are now looking at the fourth issue of the brochure “Doing Agribusiness in Ukraine” which has already become a guide on agro-industrial complex of our country.

In recent years the world of agrarian business have managed to pass the way from unlimited optimism in view of food prices during the world food crisis in 2006-2007 towards wet blanket of global financial crisis and post-crisis timid search for points of growth. Traditionally high riskiness of agricultural production in recent years has been accompanied with significant macroeconomic uncertainty in respect of some currencies and even national economies.

On the one hand, agricultural production is less susceptible to such “temporary” events as soon as demand for food has always been there and it will maintain in the future. On the other hand, sustainability of business depends upon appropriate reaction to many factors, even to those which look unimportant at the first glance.

We do not hope that we will be able to provide answers to all questions associated with agricultural and food sphere, but we do hope that our complex presentation of the agro-industrial complex of Ukraine against the background of new challenges and phenomena will be useful for our readers.

We are very pleased that preparation of this issue of “Doing Agribusiness in Ukraine” was done in close cooperation with partners of Association “Ukrainian Agribusiness Club” (UCAB). Such cooperation has already become a tradition; moreover, in the last years UCAB implemented several projects aiming at improvement of efficiency of agrarian companies in Ukraine.

We hope that further development of agrarian sector will be accompanied with corporate achievements of members of the Association, of our partners as well as of agricultural business as a whole!

President of UCAB  
Alex Lissitsa

A handwritten signature in blue ink, appearing to read 'Alex Lissitsa', written in a cursive style.



## 1. Ukraine: key features of the country

### 1.1. Introduction

Agri-food business in Ukraine is one of the few sectors of the economy that successfully survived global economic crisis of 2008-2009. Agricultural output has practically not diminished as compared to pre-crisis level, and the latter is going to be surpassed already in 2011, with moderate growth in livestock sector and relatively good harvest of main crops.

Moreover, activities of 2010 secured sufficiently attractive economic results for the sector, as soon as production resources were procured at low crisis prices while prices for agricultural commodities demonstrated remarkable growth during harvesting. This effect is limited in time because resources for the harvest of 2011 have also gained in price but it allowed many farms to restore their profitability in post-crisis period.

State regulation is still one of the major factors of the development of agrarian business. While quoting of cereal export restricted adjustment of domestic prices up to the level of world prices, maintaining of principal preferential regimes of taxation for agrarians in new Tax Code (2010) will surely support attractiveness of agricultural business in the nearest future.

It is expected that in the nearest years Ukraine will implement the second stage of land reform aiming to introduce free trade with farmland. At the same time, parameters of future land market are entailing heated debates, in particular, with respect to access of foreign capital to Ukrainian land market and on corporate land ownership.

So far, investment attractiveness of the sector is ensured on account of external factors, those being global growth of food prices, tense balances, and prospects of further increase of global demand. Commodities are becoming a good alternative to money, and corporate assets originating from Ukraine are turning into good multiplier of global trends.

About that, as well as about other important tendencies of Ukraine's agri-food sector we are talking in this year issue of "Doing Agribusiness in Ukraine".

### 1.2. Political situation

As we noted in the last years' issue of "Doing Agribusiness in Ukraine", Ukraine being de-jure parliamentary-presidential republic has de-facto

turned into presidential-parliamentary upon election of Victor Yanukovich as President of Ukraine. This status quo was formalized due to the ruling of the Constitutional Court of Ukraine of September 30, 2010 No. 20-пн/2010 which dismissed political reform of 2004 and restored 1996 reading of the Constitution of Ukraine.

Therefore, Ukraine came back to the Constitution of Leonid Kuchma period providing for heavy influence of the President and somewhat reduced influence of the Parliament on issues of state recruitment arrangements and economic policies. Nevertheless, distribution of competences in this situation looks artificial and conditional in view of the fact that President and Prime-Minister belong to the same political party (Party of Regions) which also controls the Parliamentary majority.

Opportunities created by political synergy of interests have been used only in part. Among the most remarkable achievements are the adoption of a new Tax Code and implementation of administrative reform.

And when the Tax Code is to a large extent an evolutionary (rather than revolutionary) document maintaining many notorious drawbacks of the old taxation system, administrative reform took quite a different path. For example, it is providing for concentration of competences in the field of food quality and safety in the hands of one institution – State Veterinary and Phytosanitary Service. One could reasonably expect that such a step would increase effectiveness of functioning of control bodies.

On the other hand, it is obvious that not every solution in the field of administrative reform will successfully pass durability test. Among “risky” solutions there is, for example, sectoral division of standardization and technical regulation. Besides, redundancies in the course of the reform are not always supported with functional optimization, and in some case it led to deterioration of effectiveness of state machine functioning.

Implementation of other reforms (including land and pension reforms and budget-balancing increase of gas prices) has so far been suspended; one can expect that further advance will depend upon forthcoming Parliamentary elections to be held in 2012.

Some of the rules of governmental draft of law of Ukraine on land market are making good example supporting such expectations. Afraid of criticism on the part of small farmers along with leftists, drafters eliminated completely any mentioning of corporate land ownership in the draft. As a result, much advertized improvement of investment attractiveness of agrarian sector upon lifting of moratorium on sale of farmland is reflecting a stereotype rather than real legislative initiatives.

It is obvious that reforms will be assuming softer forms as Parliamentary elections approach, and further prospects will depend upon results of the latter.

### **1.3. Legal system**

#### Form of government

According to Article 1 of the Constitution of Ukraine of 1996, Ukraine is a sovereign independent democratic social and legal state. Ukraine is employing



a form of government that combines features of presidential and parliamentary republic. This form of government features the following characteristics: The President of Ukraine is elected through direct universal suffrage for the term of 5 years; the President with consent of the Parliament appoints the head of Cabinet as well as ministers by recommendation of the Prime-Minister; the Cabinet is responsible to President and controlled by and accountable to the Parliament.

#### Judicial system

Today the judicial system of Ukraine comprises of the Constitutional Court of Ukraine and courts of general jurisdiction. The main task of the Constitutional Court is administration of constitutional justice and safeguarding of supremacy of the Constitution of Ukraine as the Fundamental Law.

The system of court of general jurisdiction consists of local courts, courts of appeal, higher specialized courts and Supreme Court of Ukraine. The list of specialized courts includes economic and administrative courts which administrate justice according to special procedural codes (Economic Procedural Code and Administrative Procedural Code respectively). Higher specialized courts are Higher Specialized Court for Adjudication in Civil and Criminal Matters, Higher Economic Court and Higher Administrative Court.



#### Land legislation

Legal matters related to use of land is regulated by the Constitution of Ukraine, Land Code of Ukraine (2001), Civil and Economic Codes of Ukraine (2003), Laws of Ukraine “On Land Management», «On Lease of Land», «On Estimation of Land», «On State Expertise of Land Management Documentation», «On Amelioration of Land», «On State Control Over Land Use and Protection», «On Separation of Land of State and Communal Ownership», «On Protection of Constitutional Rights of Citizens to Land», «On Procedure for Allocation in Kind (on Surface) of Land Plots to Owners of Land Shares” and other Laws and by-laws.

Land legislation of Ukraine provides for private ownership of land (including corporate land ownership) along with state and municipal ownership. At that, actual separation and titling of state and municipal land has not been done yet; therefore, provisionally, before such separation, public land within legal boundaries of settlements is administrated by local elected councils (of villages,

towns and cities) while public land beyond legal boundaries of settlements is administrated by local (Rayon and Oblast) state administrations.

Ownership of farmland is guaranteed. At the same time, there is a moratorium (ban) on alienation of land of agricultural use. Currently there are being prepared and debated drafts of legislative acts aiming at abolition of the moratorium and introduction of free market circulation of farmland. The main acts in this respect are the Laws of Ukraine “On Land Market” and “On State Land Cadastre” (the latter was upheld by the Parliament of Ukraine in the first reading shortly before release of this issue of “Doing Agribusiness in Ukraine”).

#### Agrarian legislation

The foundation of agrarian legislation of Ukraine, besides general rules of civil, economic and land legislation, is laid by the Laws of Ukraine “On Farming”, “On Priority of Social Development of Countryside and Agro-Industrial Complex of Ukraine”, “On State Support to Agriculture of Ukraine”, “On Agricultural Cooperation”, “On Grain and Grain Market of Ukraine”, “On State Regulation of Production and Realization of Sugar”, “On Pesticides and Agrochemicals”, “On Personal Peasant Farm”, “On Seed”, “On Pedigree Cattle Breeding”, “On Plant Quarantine”, «On Quality and Safety of Foodstuffs and Food Raw Materials” and some others.

Agrarian relations had reached the post-reform period of development as soon as on the basis of former collective agricultural enterprises (hereinafter referred to as CAE) new economic entities were founded; in many cases, they cultivate land leased from former members of CAE. These new entities are companies (mostly limited liability private companies, sometimes joint-stock companies); farmers; personal subsistent farms of citizens. Besides, agricultural production may be organized as a private (personal) entrepreneurship activity, production or servicing cooperative.



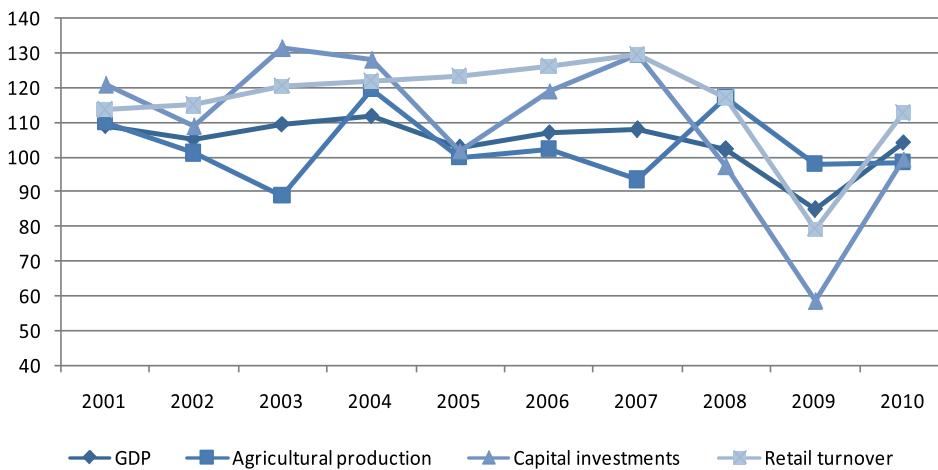


## 2. Economy of Ukraine in Post-Crisis Period

### 2.1. Main Macroeconomic Indicators

The year 2010 in Ukraine may be qualified as a period of post-crisis stabilization. As compared to 2009, which brought about significant reduction of country's GDP (by 14.8%) due to global financial crisis, in 2010 Ukraine reported growth of GDP by 4.2%. The agrarian sector demonstrated stability, just like during the crisis, and managed to ensure the level of production nearly equal to that of the preceding year.

There was some recovery in retail, and capital investments climbed up to pre-crisis level of 2008 (see Figure 2.1).



**Figure 2.1. GDP, gross agricultural output, capital investments and retail trade (in comparative prices of 2007, in % to preceding year).**

Source: State Statistics Committee

Among positive signs of 2010 there are slowing down of the rate of inflation, reduction of official level of unemployment, growth of gold and currency reserves of the National Bank of Ukraine (NBU) as well as stabilization of NBU discount rate, and decrease of interest rates of commercial banks (first of all on loans issued to legal entities).

Nevertheless, there are several negative moments. These are first of all a high debt load of the national economy and negative balance of trade. According to NBU, foreign debt of Ukraine in 2010 added USD 13.9 billion (i.e. grew by

13.5%) and reached the level of USD 117.3 billion. But compared to GDP, this debt has somewhat decreased (85.7% as compared to 89.0% in the last year). The volume of short term foreign debt by remaining maturity increased by USD 8.5 billion and by the end of 2010 made up USD 47.3 billion. The level of coverage thereof by international reserves grew up to 73% year-end (as compared to 68% reported at the beginning of 2010).

The list of factors bringing about negative trends and developments looks traditional and includes export of produce with low level of value added, poor energy efficiency, and low spending power of population as well as lack of qualified labor force.

Aggregate data on main macroeconomic indicators of Ukraine are presented in Table 2.1.

**Table 2.1. Main macroeconomic indicators of Ukraine**

	2006	2007	2008	2009	2010
<b>Gross domestic product, UAH billion</b>	544,2	720,7	949,9	914,7	1094,6
<b>Agricultural output, UAH billion</b>	94,3	113,1	154,4	157,2	184,9
<b>Capital investments, UAH billion</b>	125,3	188,5	233,1	151,2	150,7
<b>Financial results of operations of enterprises before tax, UAH billion</b>	76,3	135,9	9,0	-31,6	46,5
<b>Average nominal wages and salaries, UAH</b>	1041,4	1351,0	1806,0	1906,0	2239,0
<b>Real wages and salaries index, to December of preceding year, %</b>	111,7	110,3	97,0	99,1	110,5
<b>Income of population, UAH billion</b>	472,1	623,3	856,6	897,7	1101,0
<b>Consumer price index, to December of preceding year, %</b>	111,6	116,6	122,3	112,3	109,1
<b>Industry producers price index, to December of preceding year, %</b>	114,1	123,3	123,0	114,3	118,7
<b>Official unemployment (year-end), %</b>	2,7	2,4	2,1	2,5	1,6
<b>Export of goods and services, USD billion</b>	38,4	49,2	67,0	39,7	63,2
<b>Import of goods and services, USD billion</b>	45,0	60,7	85,5	45,5	66,2
<b>Ratio of servicing foreign debt, %</b>	17,3	18,0	18,9	44,7	40,5
<b>Gross gold and currency reserves, expressed in months of future import of goods and services</b>	3,7	3,9	6,4	4,9	

Source: State Statistics Committee





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## 2.2. Collaboration with IMF

Ukraine has nearly always resorted to collaboration with International Monetary Fund (IMF) when economic situation required so. The country does not enjoy a firm economy and may not impress with stability, especially when external economic challenges are escalating and accentuating internal problems. It is remarkable that two most devastating crises in Ukraine unfolded under the influence of the Russian crisis of 1998 and global economic crisis of 2008-2009. In general, one may discern some 10-year cycle at the beginning of which devaluation of national currency is conditioning improvement of competitiveness of the national economy, but later on structural deficiencies and problems of state adjustment bring about the next turn of the crisis.

Accordingly, collaboration with IMF under such condition may not be underestimated. In our opinion, there is another, hidden, motive behind the collaboration with IMF, namely, attempts to employ requirements of IMF as a driver of painful reforms in the country.

In general, demands of IMF are focusing on ensuring macro-financial stability and recently have been mostly directed towards reduction of budget deficit. Among such demands, there are retirement pension reform (review of the retirement age) and increase of natural gas prices for population in order to secure debt-neutral budget of "Naftogas of Ukraine". The financial sector and independence of NBU is also in focus of special IMF attention.

Nevertheless, from time to time requirements of IMF have a more applied nature, from the point of view of agrarian sector. For example, in 2008 IMF suggested the abolition of VAT benefits for agricultural producers (in order to replenish state budget) and lifting of moratorium of sale of farmland. However, those measures were not implemented. Besides, there was information that in 2010-2011 the IMF mission to Ukraine drew attention of Ukrainian authorities to the necessity of a more transparent administration of export quotas on cereals. Thus, IMF requirements still play a fairly important role in economic policy of Ukraine.

Though Mr. Mykola Azarov, Prime-Minister of Ukraine, has already mentioned that IMF financial support to Ukraine at the current stage was dispensable, these words shall be taken rather like an introduction to further negotiations with IMF about the next tranches.

Despite the fact that provision of next loans of IMF is currently not that critical for Ukraine and reserves of NBU reached the unprecedented level of USD 39 billion, the problem of currency stability is still on Ukraine's



agenda. The balance of trade is still negative, and the peak of repayment of foreign debts and retirement of governmental bonds is falling upon 2012-2013. It is obvious that these facts will condition limited budget capability in the following years (including support to agricultural producers) as well as maintaining of sensitivity of Ukraine's currency market to external challenges.

**Table 2.2. Expected payments of Ukraine to IMF, SDR million\***

	2011	2012	2013	2014	2015
<b>The principal</b>		2234,38	3656,25	2390,63	968,75
<b>Interest</b>	186,27	240,35	144,02	42,49	16,27
<b>Total</b>	186,27	2474,72	3800,27	2433,11	985,02

\*SDR – special drawing rights, current exchange rate is USD 1.58-1.62 per SDR (May 2011)

Source: IMF official web-site

### 2.3. Free trade: EU vs. Customs Union?

In view of the generally recognized opinion that full realization of Ukraine's agrarian potential is impossible without broadening of its presence on foreign markets, the processes of further international integration play an important role from the point of view of prospects of country's agriculture.

At that, Ukraine has already gained some experience regarding WTO accession when considerable reduction of customs duties led to significant increase of volumes of import. And only massive 60-percent devaluation of Hrivniya in autumn of 2008 managed to stop negative trends and restore competitiveness of national producers, in particular, producers of animal products.

The structure of foreign trade in agricultural output and foodstuffs shows that Ukraine has two major trade partners, namely Russia and EU. As a matter of fact, vectors of economic integration are aiming in the same directions.

Ukraine has already concluded free trade agreements with CIS countries. At the same time, these agreements provide for some exemptions from free trade regime; for example, it is not applied to sugar in relations with Russia, and oil supplied to Ukraine from Russia is taxed with export duty. Also, restrictive effect shall be attributed to non-tariff measures of regulation, for example, sanitary control exercised by Russia's authorities in respect of dairy and meat products of Ukrainian origin.

Some hopes on liberalization of trade regime could have been cherished in view of signing of a free trade agreement in the framework of CIS initially planned for May 2011. But signing of this treaty was postponed and, secondly, trade partners of Ukraine (first of all, Russia) link liberalization of trade regime to Ukraine's accession to Customs Union of Russia, Kazakhstan and Belarus. Among other things, such step is associated with partial transfer of economic sovereignty to supra-national bodies (for example, setting up conditions of trade with third countries).

The agreement on free trade that is currently being negotiated with the EU does not require from Ukraine such drastic steps, although the level of liberalization of trade depends, among other things, on Ukraine's readiness to adjust national legislation and procedures to rules and practices of the EU.

Negotiations with the EU are developing in a rather tense manner. Main stumbling blocks have not changed in the last year – these are tariff regulation of market access, protection of geographic names and application of export duties.

Foreign trade in agricultural goods and foodstuffs may be largely influenced by lifting of tariff protection of markets. Standpoints of parties on prospective level of tariff protection of domestic markets differ considerably.

First of all, it is true in respect of tariff quotas for import of Ukrainian goods to the EU within the framework of preferential regime. It is obvious that tariff issues will be decided upon in complex with concessions in respect of other issues of negotiations.

**Table 2.3. Possible regime for export of Ukrainian goods to EU within FTA**

Commodity	Possible parameters of import of Ukrainian goods to EU *
<b>Meat of bovine animals</b>	Quota of 6-24 thousand t with zero customs duty
<b>Pork</b>	Quota of 15-50 thousand t with zero customs duty
<b>Poultry</b>	Quota of 10-80 thousand t with zero customs duty
<b>Cereals</b>	300 thousand t – 2 million t with zero customs duty**

\* - ranges are reflecting differences in positions of negotiating parties

\*\* -in addition to quota on import from third countries to EU with application of preferential (reduced) import customs duty

Source: information of UCAB on the ground of own estimates and questioning of Ukrainian companies

It is also possible that Ukraine, in return for concessions on the part of EU, will agree to abolish and/or reduce duties on some commodities. For example, customs duty may be decreased by 20%, from 10% to 8%. However, under conditions when import duty on most items is significantly lower than VAT rate, this step is unlikely to bring about any remarkable developments in foreign trade.

There may be distinguished following important aspects of negotiations with EU:

- EU is defending its right to provide state support at a scale provided for by its agreements with WTO;
- it is very likely that EU will maintain export subsidies, at least, in respect of most commodity items;
- EU will likely ensure protection of all geographic names that have been registered in EU, except for Cahors wine.

The issue of Ukraine’s export duties has not been decided yet. Europeans insist on the abolition of export duties in mutual trade, but the agreement could provide for some exemptions in case of excessive export of some commodity items in respect of which export duties were applicable before conclusion of the agreement.

The current status of negotiations on free trade with EU is featuring reserved attitude of EU and somewhat more enthusiastic attitude of Ukraine striving for achieving progress in the negotiation process.



**Alexander Petrov, Chairman of Supervisory Board of “Industrial Milk Company”**

«Industrial Milk Company” (IMC) is an integrated agrarian business engaged in crop growing, dairy cattle breeding and potato cultivation. The land bank of the company accounts for 38 thousand ha. IMC needs for storage facilities are fully covered by own grain elevators with simultaneous storage capacity of 172 thousand t and potato warehouses capable of storing up to 10 thousand t. In 2010, IMC harvested 117 thousand t of cereals and oil crops, 6 thousand t of potato and 98 thousand t of green mass.

IMC is one of the largest milk producers in Ukraine. The population of dairy cattle owned by the company accounts for 5.6 thousand heads, including 3 150 cows. In 2010, the company produced 16 thousand t of milk.

In 2010, IMC managed to increase its income up to USD 34.8 million and net profit – up to USD 14.8 million, EBITDA made up USD 16.5 million.

In 2011, upon initial placement of shares at IPO market, IMC achieved high ratio of company value to its profit and landholding. IMC raised PLN 80.730 million (USD 29.699 million) by placing 24% of its shares at Warsaw Stock Exchange (WSE). The number of placed shares amounted to 7.475 million, including 6.5 million new shares and 0.975 million shares of redistribution option. Price of placement made up PLN 10.8 apiece.

Shares of Industrial Milk Company S.A. (Luxembourg), of IMC holding company, were placed on WSE on May 4, 2011. Funds attracted during emission of shares will be used for realization of investment plan providing for enlargement of business scale while maintaining high effectiveness. IMC is planning to broaden its land bank up to 126 thousand ha by 2016, to purchase new agricultural equipment and machinery, expand its grain storage facilities up to 130 thousand t and potato warehouses up to 80 thousand t.



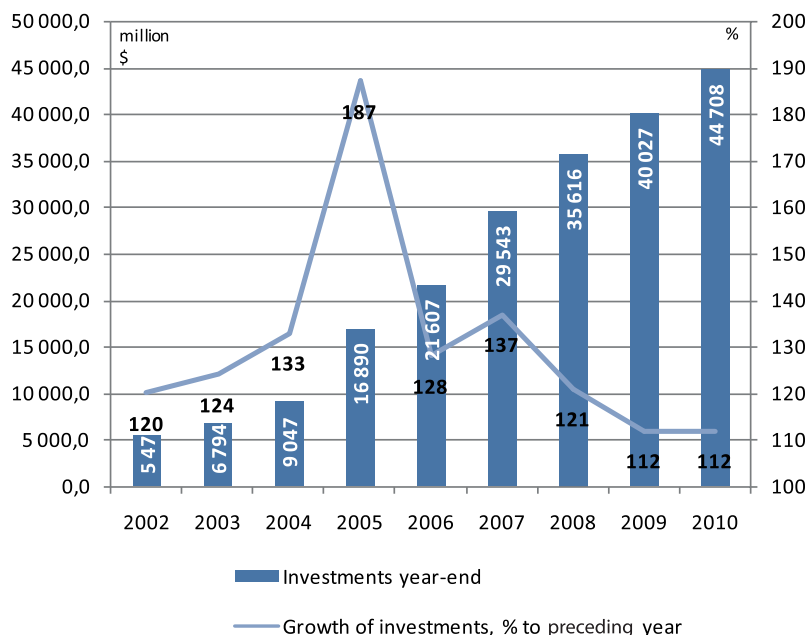
## 2.4. Investment Climate

Inflow of foreign investments to Ukraine depends on the level of political stability in the country. So, while in the first quarter of 2010 (immediately after Victor Yanukovich becoming President of Ukraine) foreign investors were taking the length of foot of new government, there has been growth of foreign direct investments (FDI) by 2% in the first quarter of 2011. Therefore, by April 1, 2011, aggregate volume of FDI in economy of Ukraine amounted to USD 45602.3 million or USD 998.1 per capita (as compared to USD 976.6 per capita as of the beginning of the year).

Nevertheless, the level of FDI per capita is still very low as compared with other countries of Eastern Europe. According to experts, main barriers to foreign investments are corruption (including corruption in court system), weak culture of law enforcement agencies as well as reproachful regulatory procedures.

In 2010, Ukraine managed to attract USD 4.68 billion of FDI (106.1% to the level of 2009). Aggregate sum of FDI by January 1, 2011 amounted to USD 44.7 billion or 12% above the last year figure. The geography of main investors looks familiar: Cyprus (USD 9.91 billion), Germany (USD

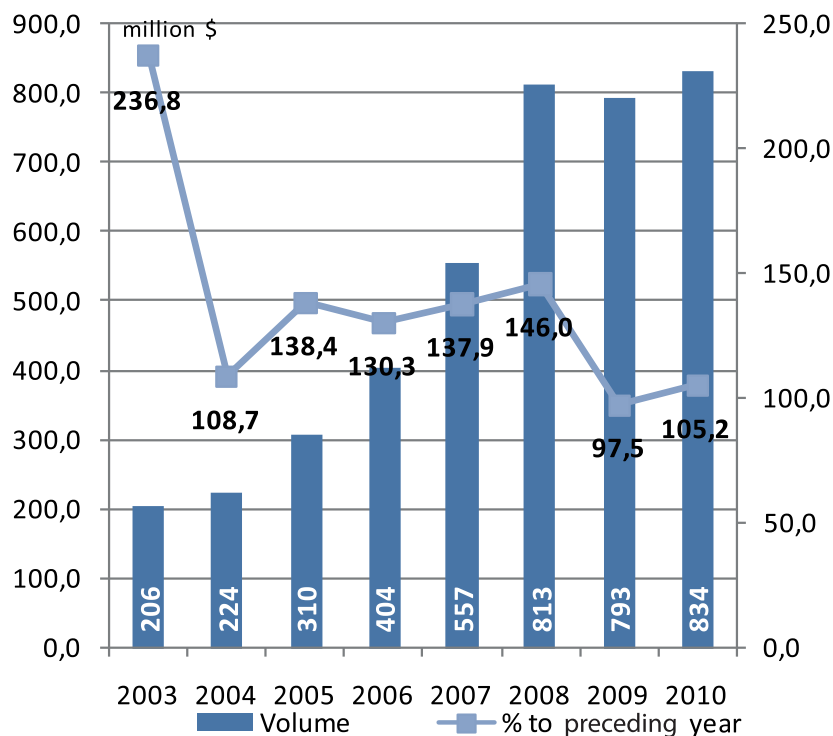
7.08 billion), Netherlands (USD 4.71 billion), Russian Federation (USD 3.40 billion), France (USD 2.37 billion) and Great Britain (USD 2.30 billion).



**Figure 2.2. Dynamics of FDI in Ukrainian economy**

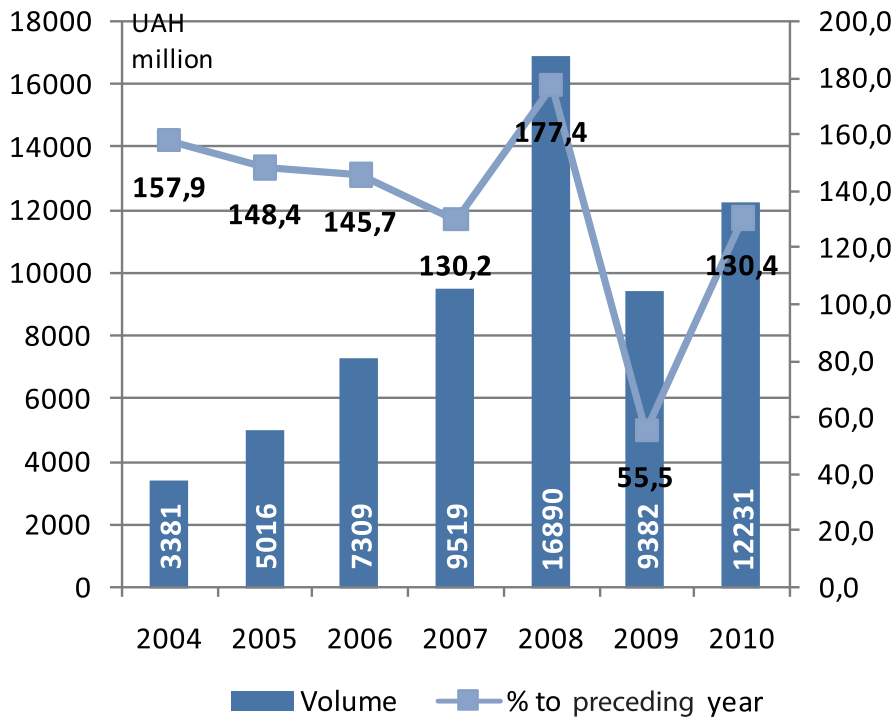
Source: State Statistics Committee

As regards the agrarian sector, in 2010 it proved its attractiveness for investors; FDI as well as capital investments grew and made up 105.2% and 130.4% to the level of 2009, respectively. Detailed information about volumes of investments is presented in Figures 2.3 and 2.4.



**Figure 2.3. Investments into agriculture, forestry and hunting**

Source: State Statistics Committee



**Figure 2.4. FDI in agriculture**  
Source: State Statistics Committee

Investments into agricultural business in Ukraine are additionally hampered by incomplete land reform, unpredictable state support and agrarian policy (e.g. introduction of export quotas on cereals). However, in the beginning of 2011, agrarian investors received quite clearly positive signals; for example, government started talking about lifting of moratorium on sale of farmland on January 1, 2012, and governmental draft of the law of Ukraine “On Land Market” became a subject of public scrutiny. Besides, there was drafted (though only in part) a procedure for financial support of livestock sector on account of VAT payable by enterprises of food industry.

The grain sector is also observing development of tools aiming at stabilization of the sector taking into account interests of business and issues of food security. In particular, much criticized export quotas have been replaced by export duties as more comprehensive and pro-competition instrument. At the same time, export tax may well lead to reduction of profitability of production of cereals.

### 2.5. Income of population

In contrast to 2009, nominal as well as real incomes of population have been growing in 2010. Besides, against the background of low inflation (9.1%) there was an increase of the rate of growth of nominal wages which made up 17.5% at the end of the year. Nevertheless, post-crisis cooling down of labour market is still felt, and consumers due to limited earnings switched to cheaper commodity segments. Information on incomes of population and nominal wages is presented in Figures 2.5 and 2.6.

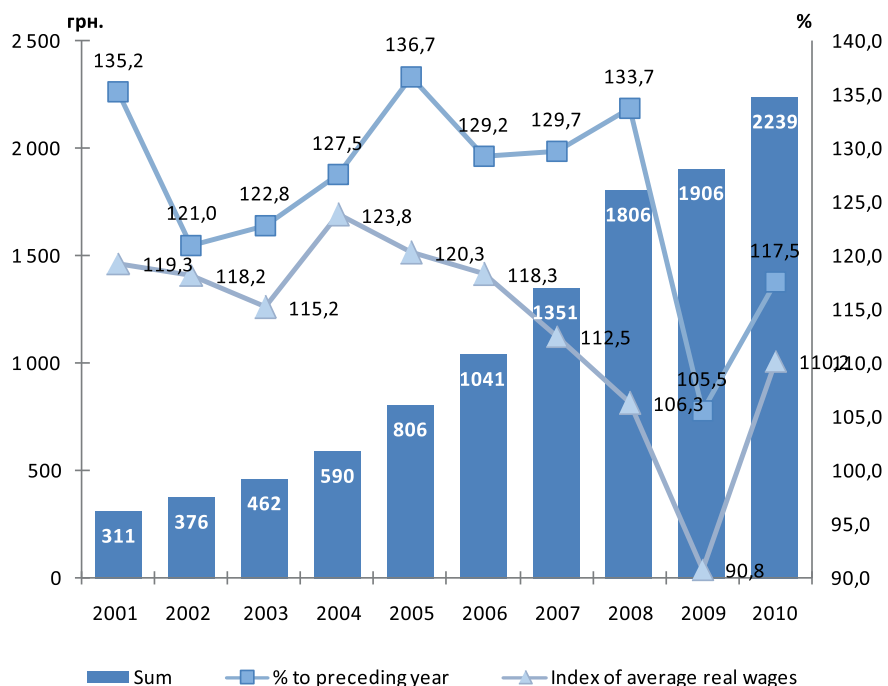


Figure 2.5. Dynamics of monthly nominal wages

Source: State Statistics Committee

As regards structural changes, 2010 witnessed a slight growth of income generated by property. At the same time, the share of savings in the structure of expenses grew from 9 up to 14% (mostly due to reduction of consumption of goods and services). The latter may be explained by high uncertainty and desire to improve personal financial durability towards possible risks.

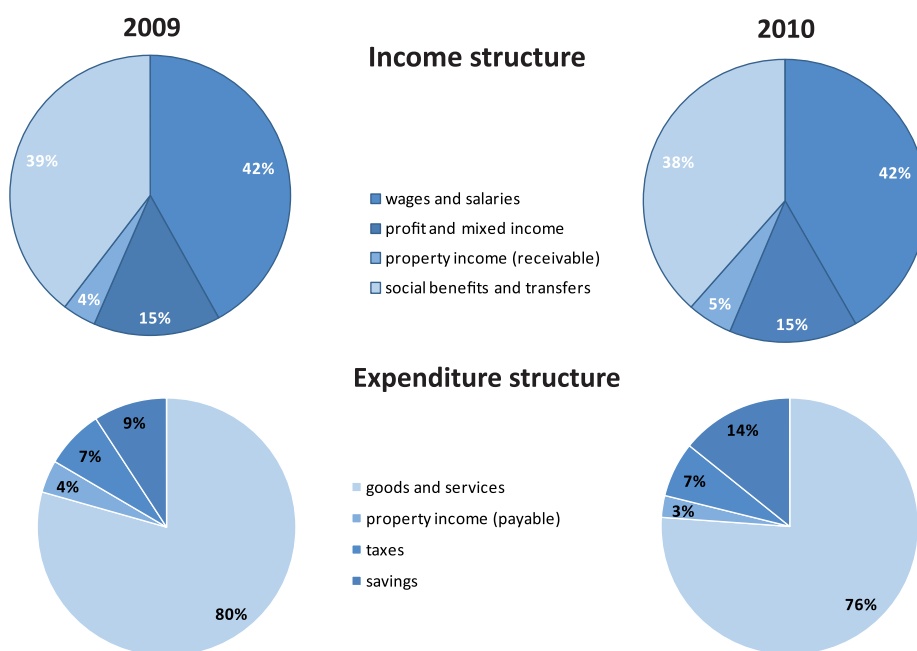


Figure 2.6. Dynamics of and structural changes in incomes of population of Ukraine

Source: State Statistics Committee



## 2.6. Financial and credit system

Ukraine has a two-tier bank system consisting of a central bank, on one hand, and commercial banks and non-bank finance and credit institutions, on the other hand.

The National Bank of Ukraine (NBU) is administrating single state policy in the field of money turnover, regulation of exchange rate, emission and coordination of the whole banking sector; it also discharges some other functions in finance and credit sphere.

One of the monetary tools employed by NBU for indicating possible value of resources is the discount rate. It depends on processes taking place in macroeconomic and budget spheres and on the money market.

Dynamics of NBU discount rate show some stabilization of this indicator starting from August 2010 at the level of 7.75% (see Figure 2.7). No doubt this indicator is not as important in Ukraine as in many other countries, and there have been periods when this indicator had purely nominal meaning. However, its role could be more important for agriculture as soon as compensation payments under the program for reimbursement of interest rates in the agro-industrial complex are calculated on the basis of NBU discount rate.

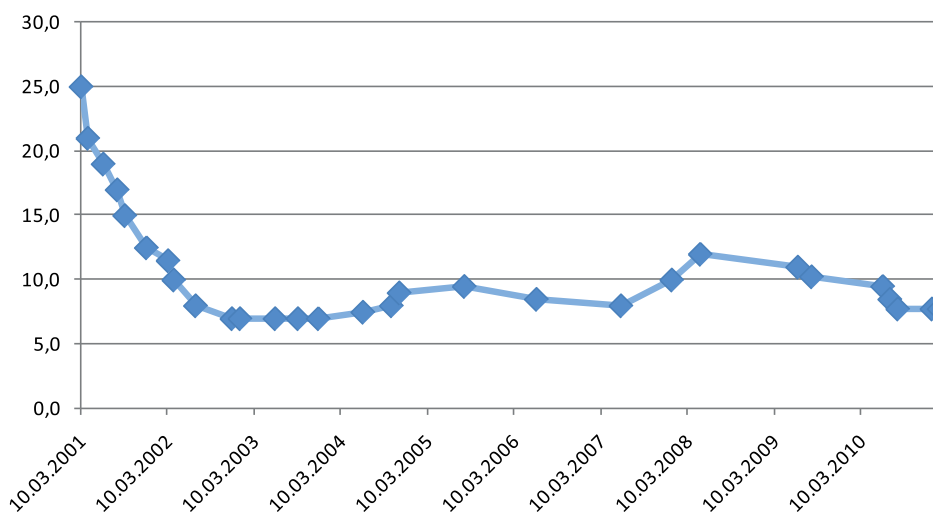
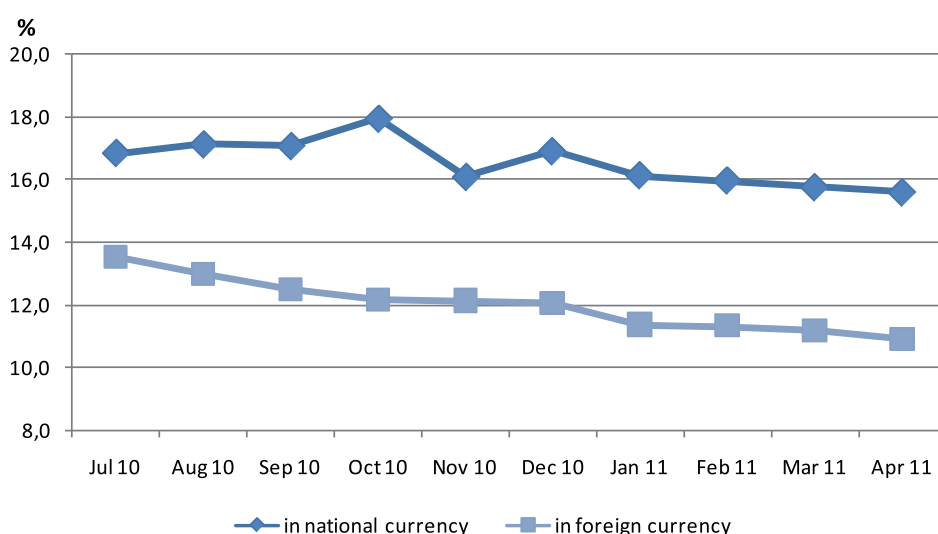


Figure 2.7. Dynamics of NBU discount rate, %

Source: NBU bulletin, February 2011

Nevertheless, despite strengthening of the exchange rate and absence of serious devaluation threats (at least in the short-term perspective), high risks are brought about by high debt load of Ukraine's economy. Ratio of loans to GDP exceeds 80%. For reference: this indicator makes up 30-40% for Turkey and most CIS countries. Persistent deficit of trade balance is also generating hypothetic risks likely to materialize when coupled with other destabilizing factors. According to NBU, crediting of legal entities (non-financial corporations) looks as follows. The average interest rate in 2011 on long-term loans accounts for 15.9% and 11.2% (in national and foreign currencies<sup>1</sup> respectively). Between July 2010 and April 2011, this indicator demonstrated decrease from 16.8% down to 16.5% for loans in national currency and from 13.5% down to 10.9% for loans in foreign currency (see Figure 2.8).



**Figure 2.8. Average interest rates on long-term loans issued by commercial banks to businesses<sup>2</sup>, 2010-2011**

Source: NBU bulletin, April 2011

At the same time, according to the State Statistics Committee, the debt load of agrarian sector to its gross output accounts for only 34%. The ratio of the same to assets of agricultural enterprises accounted for 18% as of January 1, 2011 (while the total sum of loans issued to agrarians made up UAH 27 billion).

In view of the growth of loans in the first quarter of 2011, we may assume that banks in general are ready to issue loans to agricultural producers, but reduction of cost of resources has recently stopped. It is possible that in view of the growth of liquidity of the bank system banks are interested in attraction of new clients, and additional risks associated with less reliable borrowers are reflected in interest rates. If we look at the interest rates on state bonds (9-11% for the period over 1 year), the reserves for further reduction of interest rates for large reliable borrowers are still available.

<sup>1</sup> Due to accentuation of public debates on expected lifting of moratorium and opening of farmland market it is necessary to point out that one of the most important pricing factors is the situation of the credit market. This issue is analyzed in details in the UCAB study "Market Value of Arable Land in Ukraine" (2011).

<sup>2</sup> Cost of loans – aggregate sum of remuneration (real payment for loan) provided for by loan agreement and including interest rate, any other commissions, fees set up in lump sum or in percent payable by a borrower to lender due to the fact of initiation, provision, servicing and repayment of loans.



As of the beginning of 2011, there were 194 commercial banks in Ukraine, the net assets of which amounted to UAH 942.1 billion and liabilities to UAH 804.4 billion. The share of foreign capital in Ukrainian banks made up 40.6%.

**Table 2.7. Assets of the largest Ukrainian banks as of January 1, 2011**

<b>№</b>	<b>Name</b>	<b>Assets</b>	<b>Own capital</b>	<b>Liabilities</b>
<b>1</b>	PRIVATEBANK	113 437 222	11 879 967	101 557 255
<b>2</b>	UKREXIMBANK	73 171 643	17 454 296	55 717 348
<b>3</b>	OSCHADBANK	59 019 133	16 626 329	42 392 804
<b>4</b>	RAIFFEIZEN BANK AVAL	55 100 385	6 441 276	48 659 109
<b>5</b>	UKRSIBBANK	46 128 187	4 855 443	41 272 744
<b>6</b>	UKRSOTSBANK	41 603 497	6 570 187	35 033 310
<b>7</b>	PROMINVESTBANK	34 612 855	4 589 742	30 023 113
<b>8</b>	VTB	33 144 592	4 343 421	28 801 172
<b>9</b>	ALFA-BANK	26 594 816	3 121 193	23 473 623
<b>10</b>	OTP	24 681 819	3 436 974	21 244 845

Source: NBU

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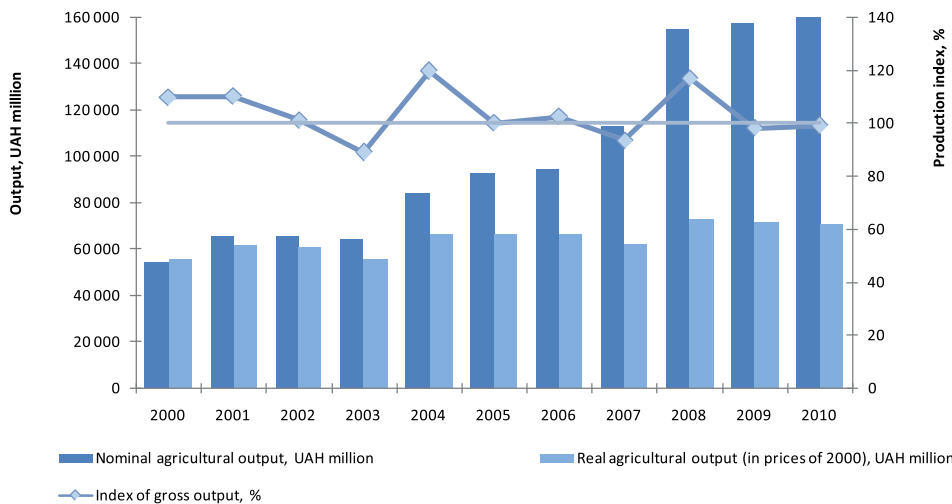


### 3. Agriculture of Ukraine

#### 3.1. Agricultural production

##### 3.1.1. General description

Over the last decade, there have been remarkable changes in Ukraine's agriculture. Increase of intensity of production, re-orientation towards more profitable crops and commodities, expansion to foreign markets, development of agrarian holdings and attraction of investments on international stock markets – all these contributed to turning of Ukraine's agriculture into the most attractive sector of the economy.



**Figure 3.1. Gross agricultural output of Ukraine**

Source: State Statistics Committee

The best evidence of sector's development is the fact that it increased its output by 27% (starting from 2000) without expansion of crop areas (see Figure 3. 1.). At the same time, low productivity, outdated physical infrastructure and technologies, lack and high cost of lending resources, ineffectiveness of management and state agrarian policy missing predictability have prevented stable growth at high rates.

##### 3.1.2. Crop growing

###### Cereals

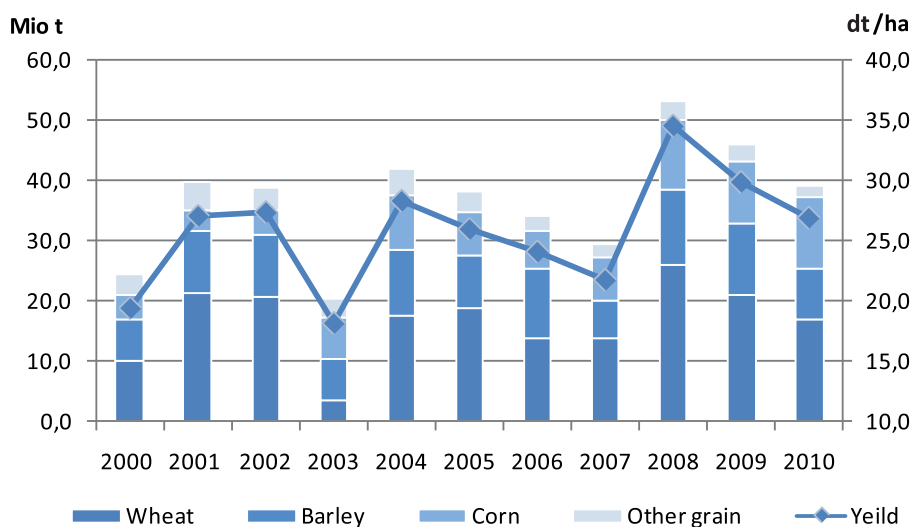
Cereal crops are the backbone of Ukraine' crop growing; in 2010, areas under cereal crops accounted for 57% of the total area under crops. Gross harvest of cereals in recent years is varying from 40 to 50 million t (see Figure 3.2). Main crops are wheat, corn and barley upon which over 90% of gross harvest is falling.

In the nearest future, cultivation of cereals will retain the position of the main sector of crop growing. Increase of yields of cereals and leguminous crops may secure further improvement of harvest up to the level of 70-80 million t. This expectation is supported by overall trends observed in the sector: general improvement of yields, expansion of crop areas under corn on account of areas where barley is currently harvested.

###### Oil crops

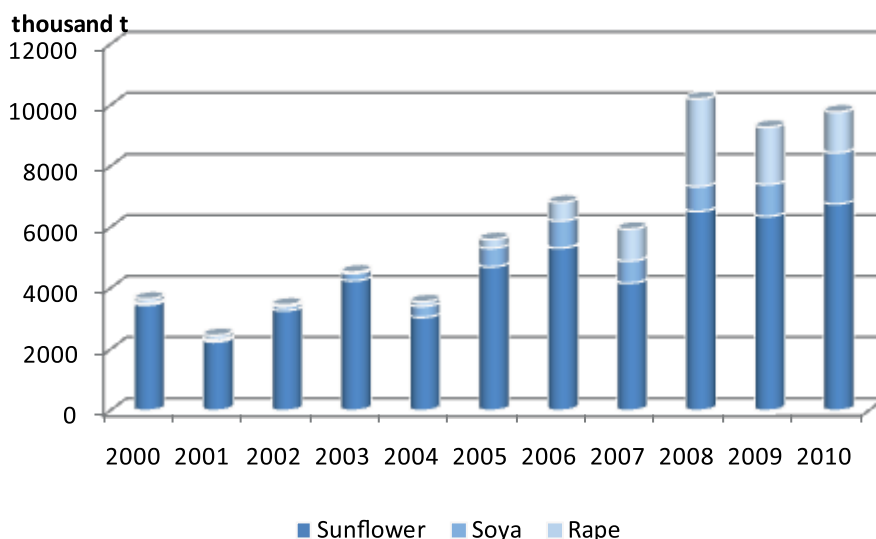
Production of oil crops has been actively developing in recent years, on account of improvement of yields as well as on account of expansion of

crop areas. Gross harvest of sunflower seed in 2010 reached the record level of 6.77 million t; good results were attained in cultivation of soybeans (1.68 million t, see Figure 3.3 for details). Improvement of production in the sector of oil crops has been mostly driven by high profitability.



**Figure 3.2. Gross harvest of cereals and leguminous crops in Ukraine, million t**  
Source: State Statistics Committee

Nevertheless, further expansion of areas under sunflower will likely be limited due to administrative regulation of crop rotations. Respectively, production may be enhanced only on account of better yields. Cultivation of soya which demonstrates good profitability and does not exhaust soil will be most likely further expanded, especially in the south of Ukraine.

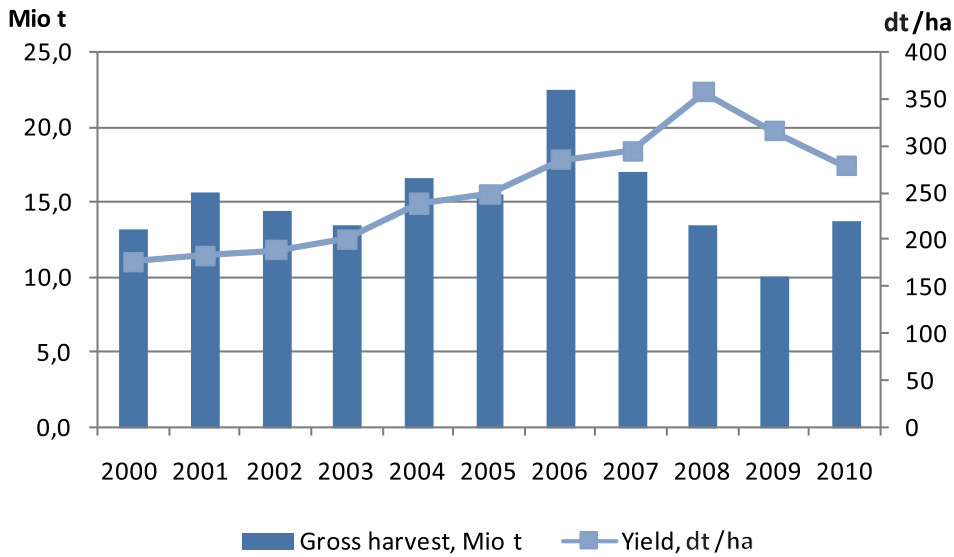


**Figure 3.3. Gross harvest of oil crops in Ukraine, million t**  
Source: State Statistics Committee

### Sugar beet

Sugar beet is an important crop for Ukraine's agriculture because sugar produced from sugar beet almost completely covers internal demand. It is expected that in 2011 production of sugar beet will make up 16-17 million t due to expansion of crop area up to 550 thousand ha (see Figure 3.4).





**Figure 3.4. Gross harvest of sugar beet in Ukraine, million t**

Source: State Statistics Committee

Inability of sugar beet to compete with sugar cane eliminates export prospects of Ukrainian sugar; therefore, production of sugar beet and sugar will be targeting first of all at the domestic market.

Potato

Production of potato in Ukraine has remarkable scale (18-20 million t annually), but it is by 98% concentrated in households. For agricultural enterprises, cultivation of potato is still not a priority. Nearly the same situation is observed in vegetable production: about 80% of vegetables are grown in households, at peasant subsistent farms. However, due to improvement of profitability of potato and vegetable growing, large agricultural enterprises are demonstrating increasing interest towards these activities.

**3.1.3. Livestock farming**

Meat sector

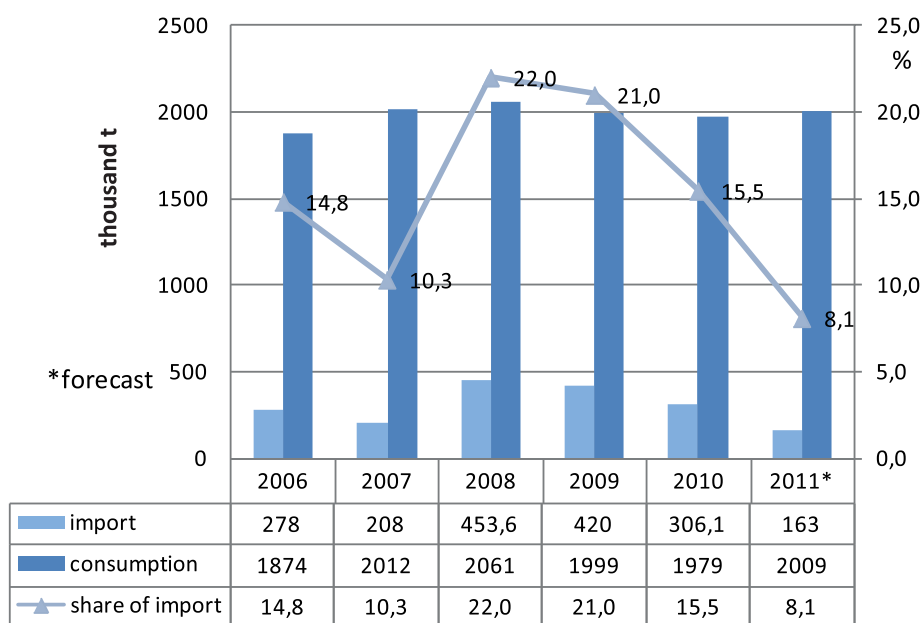
Deterioration of profitability of production of all types of meat expected in 2011 due to significant increase of fodder prices will lead to slowing down of rates of growth of production and further redistribution of meat market. According to preliminary estimates, growth of meat production in 2011 will make up about 3-4% while a year ago this indicator made up 7%. UCAB estimates that in 2011 total production of meat will reach 1930 thousand t (slaughter weight); at that, the share of poultry meat in the structure will grow up to 56% and the share of beef will decrease down to 12%. Pork is likely to keep its current place in the structure which is equal to 32%. Other types of meat are jointly holding less than 1% of the market.

Due to low spending power of the population and high cost of production of main types of meat, it is expected that further development will be observed in large vertically integrated companies which have managed to enhance their share in the overall structure of production in recent years. While several years ago such companies were found only in aviculture,

in 2008-2009 active development of agriholdings was observed in pig breeding, too.

Cattle breeding is still in deep decline, despite high procurement prices for live bovine animals, and this downward trend is supported by monthly decrease of cattle population.

In general, against the background of stable consumption of meat on internal market, there is a firm trend of reduction of import and substitution of imported meat with meat of domestic origin.



**Figure 3.5. Share of import in overall structure of meat consumption**

Source: own estimation on the basis of official statistics

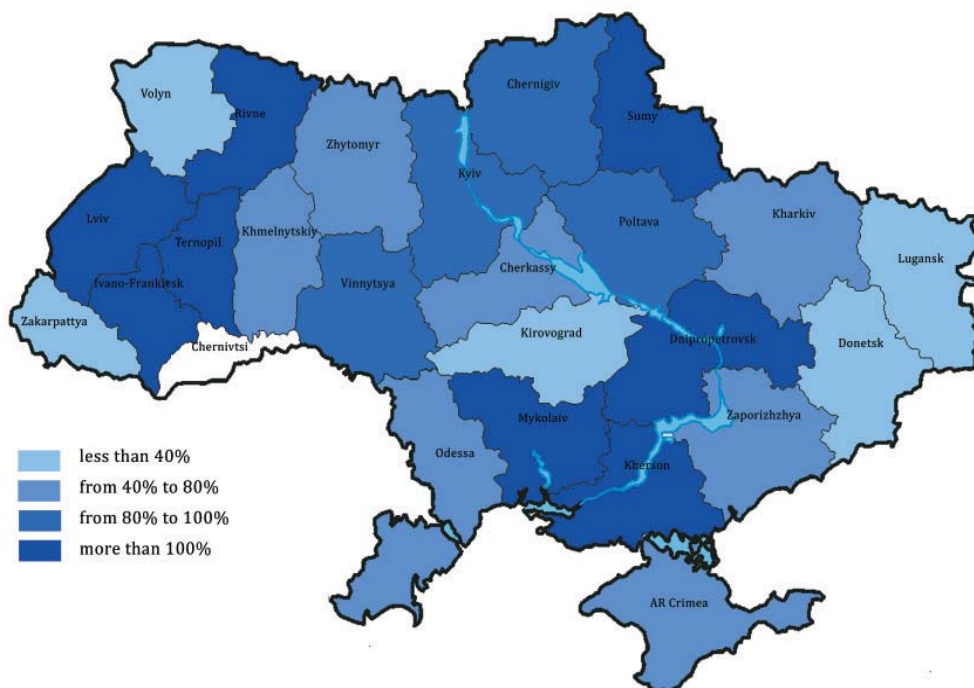
### Dairy sector

Long-lasting invariably downward trend in dairy sector – in terms of population of cows and in terms of milk production – has already led to the situation when deficit of milk for industrial processing became very acute. However, if one looks at official statistics on production of milk in households and on corporate farms and compares them with data on industrial processing by regions, it turns out that all regions do have excess of milk. But in some regions, like Mykolayiv, Kherson, Kyiv, Cherkasy, Poltava and Sumy Oblasts, competition of processors over milk may be more acute as the share of supply for processing accounts for 60%.

At the same time, if we look at production and processing of milk originating from agricultural enterprises, taking into account that the latter are constantly increasing supply, we will conclude that demand for milk from agricultural enterprises is significantly exceeding output in some regions (see Map 1).

At that, agricultural enterprises are undergoing essential structural changes. So, the group of enterprises with an annual output below 2 thousand t is reporting reduction of production while large farms are reporting increase of milk output by 8%. Unfortunately, achievements of the latter group could not make up for failure of the former.





Map 1. Share of milk supplied for processing by agricultural enterprises, % of the total production, 2010

Table 3.1. Grouping of enterprises by volumes of milk production, t/year

Range	Number of farms	Production of milk, total, thousand t	Share of group in overall output	Dynamics of output in group, %
<b>Farms, total</b>	4294	2226		
<b>annual output</b>				
<b>less than 2000 t</b>	4009	1230,7	55%	-11%
<b>2000 t and more</b>	285	995,6	45%	8%

Source: own estimation on the basis of official statistics

It is necessary to mention that in 2010 there were 22 agriholdings with an annual production of milk exceeding 5 thousand t at each of them (medium and large independent producers are not taken into consideration; see UCAB study “Largest Livestock Holdings of Ukraine: Development and Perspectives”). Their share in the overall milk output (only agricultural enterprises) accounted for 18.1%. Besides farms belonging to holdings, there were 30 independent producers with the same scale of production. Their market share slightly exceeded 13%. The trend toward enlargement and concentration has been irreversible throughout the last years.

Among positive trends, there is also an increase of the share of milk of extra quality in the overall output of agricultural enterprises<sup>3</sup>; it accounted for 7.4% in the first quarter of 2011 (against 4% in the same period of 2010). But most milk is still supplied as milk of high (35.1%) and first (53.8%)

<sup>3</sup> Large and medium producers are those having gross annual yield of milk at the level of 10 and 5 thousand t respectively.

grade. At that, households manage to supply mostly milk of the second grade (63%); less than 1% is qualified as extra quality milk.

Lack of long-term strategy for the development of dairy sector and production of milk, missing state programs for support of implementation of the said strategy along with volatility of prices, absence of long-term contractual relations between producers and processors and poor culture of discharge of contractual obligations are pushing processors towards investments into milk production. Investment projects are not limited to traditional advanced payments, provision of interest-free loans and compensation of interest rates; they also include construction of new livestock breeding complexes and establishment of servicing cooperatives in the private sector etc.

### Viewpoint



#### **Anton Yakovenko, Director General of TERRA FOOD**

*Over a relatively brief period of operating (the company was established in 2006), TERRA FOOD company managed to become a key player of dairy and meat markets. TERRA FOOD is an integrated production and trade holding uniting 10 processing enterprises of dairy and meat sector in Ukraine, a production unit in Russia and agricomplex "Zelena Dolyna" (Green Valley).*

*The holding is an absolute leader of Ukrainian spread market and one of the largest producers of cheese (9% of the domestic market). Production facilities of the holding have capacity to produce over 77 thousand t of butter and spread, over 20 thousand t of cheese, over 55 thousand t of whole-milk products and over 35 thousand of meat and sausage products.*

*The market share of TERRA FOOD at whole-milk products market over year and a half grew from 0 to 3%. Income is growing accordingly. In the nearest future, the company is going to take over 5-6% of whole-milk products market.*

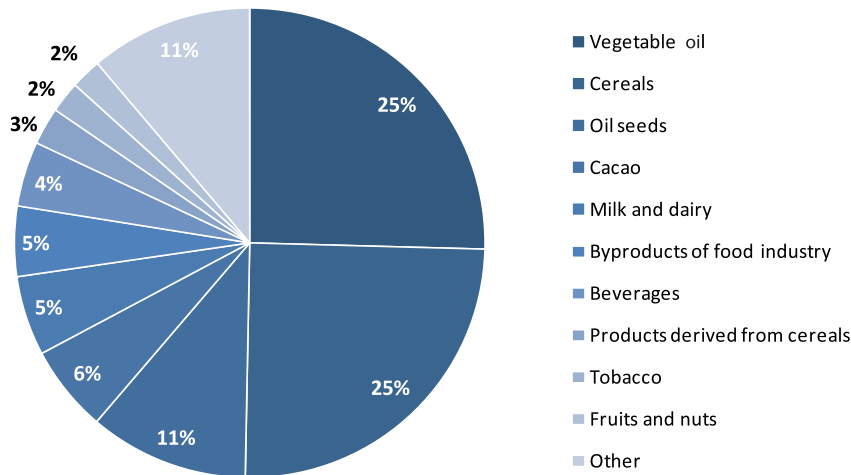
*Foodstuffs produced by enterprises of TERRA FOOD are successfully exported to CIS countries and worldwide. Company promotes its well-known trademarks and brands: Tulchinka, Premialle, Bila Linia etc.*

*Enterprises of TERRA FOOD employ certified systems for ensuring quality control ISO 9001, food safety ISO 22 000 and environmental management ISO 14001.*

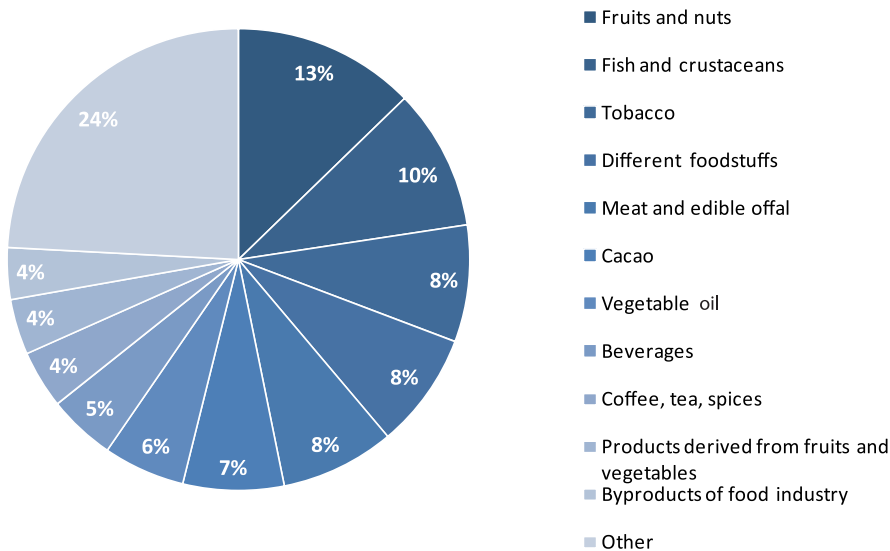
### **3.2. Foreign Trade**

The structure of foreign trade of Ukraine once again confirmed the importance of agro-industrial complex for national economy – 19.3% of export in 2010 fell upon agricultural commodities and foodstuffs. Though Ukraine is exporting agricultural goods to all continents, main trade partners are member states of the EU, CIS countries and countries of Middle East. Ukraine has effective free trade agreements with all CIS countries, and it is expected that a free trade agreement will be signed with the EU by the end of 2011.

The structure of foreign trade in agricultural goods is presented in Figures 3.6 and 3.7. The volume of export in 2010 made up USD 9919 million, volume of import – USD 5763 million.



**Figure 3.6. Structure of export of agricultural output and foodstuffs in 2010, %**  
Source: State Statistics Committee

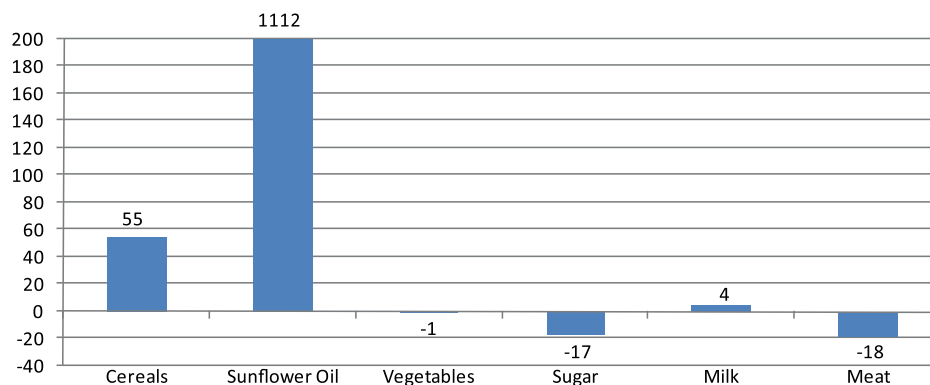


**Figure 3.7. Structure of import of agricultural output and foodstuffs in 2010, %**  
Source: State Statistics Committee

Despite significant reduction of export of cereals (by 31%) in 2010 as compared to the previous year (due to poorer harvest and introduction of export quotas), the overall agricultural export grew by 4%. The most remarkable growth was reported about export of vegetable oils and fats (46%); that compensated for restriction of cereal export. Export of dairy products also demonstrated impressive growth by 37%.

The extent to which Ukrainian market depends on international trade is presented in Figure 3.8. As we may see, markets of cereals and oil crops are significantly dependent on demand on the part of global market. Only the sugar market demonstrates dependence on import.

A different situation is observed on the meat market: according to the UCAB study “Largest Livestock Holdings: Development and Perspectives”, Ukraine may fully cover its demand for poultry meat in about three years. Demand for dairy products and vegetables is also mostly covered by domestic producers.



**Figure 3.8. Share of net trade to internal consumption in 2010, % (“+” - net export, “-” – net import).**

Source: estimates of UCAB

Speaking of certain commodity items, one has to acknowledge that in the current marketing year Ukraine has managed to retain the same position – the fourth – on global corn market, but gave up its leading position on the barley market and became the third largest supplier of this product in the world (see Table 3.2). Besides, Ukraine descended from the second to the third position in the ranking of exporters of rapeseed, having given up its place to Australia.

Traditionally, Ukraine keeps its undisputable global leadership in export of sunflower oil; this year it has also shared status of top supplier of sunflower seed with EU. In export of animal products only the cheese-making industry is providing tangible volumes of export.

**Table 3.2. Export of foodstuffs in 2010/2011 marketing year (by main exporters, thousand t)**

Corn		Barley		Rapeseed	
Country	Volume	Country	Volume	Country	Volume
USA	48262	Australia	4700	Canada	7050
Argentina	14500	EU-27	4500	Australia	1500
Brazil	8500	Ukraine	2500	Ukraine	1410
Ukraine	6000	Canada	1300	USA	262
India	2400	Argentina	1100	EU-27	220

Sunseed		Sunseed oil		Cheese	
Country	Volume	Country	Volume	Country	Volume
Ukraine	400	Ukraine	2500	EU-27	580
EU-27	400	Argentina	950	New Zealand	285
China	160	EU-27	160	Australia	165
USA	159	Russian Federation	150	USA	163
Moldova	100	Bolivia	136	Ukraine	85
Argentina	50	Turkey	80	Argentina	45

\* - forecast

Source: FAS USDA

### 3.3. Taxation<sup>4</sup>

#### 3.3.1. Tax issues in land tenure

##### Payment for land

Tax Code starting from January 1, 2011, replaced the Law of Ukraine “On Payment for Land” No. 2536 of July 3, 1992.

One of the most remarkable novelties brought about by the Code is clear definition of tax base for calculation of land tax, namely:

- normative monetary value in case valuation has been completed;
- area of parcels which do not have normative monetary value.

##### Land tax rate for farmland

Land Code defines clear rules on rates of land tax for farmland:

- for agricultural grounds (arable land, hay-fields, pastures) – 0.1% of normative monetary value;
- for areas under perennial plantations - 0.03% of normative monetary value.

For agricultural grounds allocated according to prescribed procedures and used for agricultural needs, land tax is paid by rates stated above, regardless of the category to which the said grounds are attributed (Land Code says that agricultural land may be found nearly in every category of land).

The Tax Code is also providing for tax benefits for some categories of citizens and legal entities. Among those are, for example, experimental farms of scientific and research institutions and educational establishments of agricultural profile and vocational schools, owners of land plots (land shares) who leased their plots (shares) out to agricultural producers with status of payer of fixed agricultural tax.

Besides, land tax is not paid for:

- agricultural land of radioactively contaminated areas and chemically polluted territories;
- farmland under temporary conservation or agricultural reclamation;
- land parcels of state variety testing stations used for testing of agricultural crops;
- land parcels of agricultural use of all patterns of ownership occupied with young gardens, vineyards and berry-fields till they enter the period of fruit-bearing, and also parcels under hybrid plantations, gene fund collections and nursery gardens.

##### Lease of land

Land rent, just like it used to be, is paid on the ground of contract for lease of land; at that, the Code is prescribing that minimal rate of land rent shall not be lower than the rate of land tax provided for by the Code (i.e. 0.1% of normative monetary value).

#### 3.3.2. Taxation of agricultural producers

In order to support the agrarian sector of the economy and to reduce tax pressure upon agricultural producers, legislation established special regimes of taxation for enterprises of the sector:

- alternative system of taxation – fixed agricultural tax which is building upon specifics of agricultural business;
- special regime of VAT application;

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<sup>4</sup> This section has been drafted by BEITEN BURKHARDT company (Turgenevska, 38, Kyiv, 01054, Ukraine, [www.beitenburkhardt.com](http://www.beitenburkhardt.com)).

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- special regime of VAT application;
- temporary exemption of some transactions on supply of cereals and industrial crops from VAT.

With adoption of new Tax Code which entered into force on January 1, 2011 (except for some parts which enter into force later on), there have been no fundamental changes in taxation of agricultural enterprises and application of special regimes of taxation. Below we are briefly describing these regimes under new Tax Code.

#### Fixed agricultural tax (FAT)

FAT is a tax which is calculated and paid in relation to the area of agricultural land in use (ownership) of a taxpayer as a percent of normative monetary value of land. FAT replaces the following taxes and contributions:

- corporate profit tax including advance payment in the process of dividend distribution;
- land tax for land used for agricultural production;
- contribution for special use of water resources;
- contributions for undertaking of some kinds of entrepreneurial activities (including trade activities).

All other taxes and contributions are paid by payers of FAT on the usual terms according to the Tax Code of Ukraine; single social contribution for social insurance is paid on the basis of the Law of Ukraine “On Collection and Accounting of Single Contribution for Mandatory State Social Insurance”.

The following land held by agricultural producers (in lease or ownership) are subject to FAT:

- Arable land;
- Hay-fields;
- Pastures;
- Perennial plantations;
- Land of water fund (internal water basins, lakes, ponds, water storage reservoirs).

**Table 3.3. Payers of fixed agricultural tax**

<b>Who is qualified for FAT?</b>	Enterprises meeting the following criteria: <ul style="list-style-type: none"> <li>• produce agricultural products and/or grow and catch fish in lakes, ponds and artificial water reservoirs, process the said products with use of own or leased facilities and equipment, including tolling schemes, supply agricultural products and/or fish;</li> <li>• hold farmland (own or leased);</li> <li>• share of agricultural production is equal or exceeding 75%.</li> </ul> Share of agricultural production – specific weight of proceeds from realization of agricultural products and products derived from the latter in the overall income of an enterprise
<b>Who is not qualified for FAT?</b>	<ul style="list-style-type: none"> <li>• Enterprises earned over 50% of income from selling of ornamental plants, wild animals and birds, furs;</li> <li>• Enterprises producing and/or selling items subject to excise tax (except for sale of grape wine-making materials by enterprises of initial wine-making);</li> <li>• Enterprises having tax debt on the date of application for acquiring status of FAT payer, except for bad debts appeared as a result of force-majeur</li> </ul>

The basis for calculation of FAT is the normative monetary value of agricultural land completed by July 1, 1995<sup>5</sup>.

Rates of FAT are defined in per cent to the tax base for 1 ha of agricultural land or land of water fund depending on their category (type) and location.

**Table 3.4. Rates of fixed agricultural tax**

Types of land	Rates of FAT (% of normative monetary value)		
	general	for mountain and forest areas	for areas under cover (greenhouses)
Arable land, hay-fields, pastures	0,15	0,09	1,0
Perennial plantations	0,09	0,03	-
Land of water funds	0,45	-	-

The basis period for the purposes of FAT calculation is a calendar year. Tax payers estimate the sum of tax on their own as of January 1 of a current year.

Estimated sum of FAT is divided by quarters as follows:

- I and II quarters – by 10%;
- III quarter – 50%;
- IV quarter – 30%.

Sums of FAT falling on a respective quarter are divided into three equal parts and paid on a monthly basis to a special account of a budget of the administrative district where taxed land parcel is located.

Special regime of VAT (applicable till January 1, 2018)

An enterprise operating in the field of agriculture, forestry or fisheries may choose special regime of VAT taxation provided that:

- activities of the enterprise are mostly consisting of supply of own agricultural goods (services) produced at own (leased) production facilities (including tolling schemes);
- specific weight of agricultural goods (services) accounts for no less than 75% of the overall value of goods (services) produced (provided) in 12 preceding months.

The enterprise which has chosen special regime of VAT taxation shall open a special account in the bank (current account with special regime of use); the account shall be open within one reporting (tax) period upon issue (by tax authorities) of the certificate of registration of the enterprise as a subject of special regime of VAT.

The sum of VAT accrued in transactions of supply of agricultural goods produced on own facilities (as well as goods produced in tolling schemes) is remitted by agricultural enterprises from their current accounts to their special VAT account. This sum of VAT is used for compensation of VAT paid by the enterprise from the value of production factors; if there is a leftover, it may be used for other production purposes.

VAT exemptions (supply of cereals and industrial crops)

Starting from January 1, 2011 and till January 1, 2018, the following transactions are exempt from VAT: supplies within customs area of Ukraine of cereals

<sup>5</sup> Tax Code does not provide for annual indexation of normative monetary value for the purposes of taxation.

(commodity headings 1001-1008, except for 1006 and 1008 10 00 00), of industrial crops (commodity headings 1205 and 1206), except for the first supply performed by agricultural enterprises being producers of the said commodities and crops, and also supply of wood (commodity headings 4401, 4403, 4404).

## Viewpoint

### **Meeuwes Brouwer, Agricultural Counsellor, Embassy of the Kingdom of the Netherlands in Ukraine**

*The Netherlands is famous for its windmills and tulips, of course, but there is much more to my country than that. For example, the Netherlands is the world's second largest agricultural exporter and one of the world's leaders in food and flower technology, with unrivalled expertise in genomics, functional foods, plant breeding and food and flower research. The Dutch contribute a lot to the search for solutions to key problems that all countries encounter. As one of the largest players in the world horticultural market, the Netherlands has a reputation to be proud of. Every year Amsterdam welcomes guests from all over the world at the international trade show for horticulture called Horti Fair<sup>6</sup>. From international perspective it is the most complete of horticultural trade fairs, besides being the best visited horticultural event in the Netherlands. Dutch horticulture is leading in the innovative storage and transport technologies. Potatoes and onions can now be stored for up to six months without any loss of quality. Wide use of these technologies dramatically improved food supplies in many countries around the world, including Ukraine.*

*Sustainability is another global trend that affects many aspects of consumers' lives. Production methods need to be as sustainable as possible and for this reason in the Netherlands attention is increasingly being devoted to energy efficiency and the minimization of waste of food products. The Dutch agrifood chain includes professional suppliers of planting material, seed potatoes, field machinery, climate control systems, refrigeration and freezing installations, warehouse logistics, transport systems, sorting and packing equipment and last but not least greenhouses.*



### **3.4. State support<sup>7</sup>**

BEITEN BURKHARDT

Besides tax benefits, there is also a special law providing for the state support of agriculture (effective from 2001); current reading of the said law was adopted in 2004 under No. 1877 (hereinafter referred to as Law 1877). Later on it has been edited on several occasions. This law provides for the main tools and measures of state support to production of agricultural commodities and development of agrarian market of Ukraine.

Law 1877 provides for the following functions of the state in the field of adjustment of agriculture and agrarian market<sup>8</sup>:

- regulation of prices for some kinds of agricultural goods;
- regulation of market of agricultural insurance;
- introduction, upon decision of the Cabinet, of pledge procurement of cereals subject to state price regulation;

<sup>6</sup> The Horti Fair is divided into the segments Horti Tech and Horti Grow & Trade and in 2011 it will be welcoming foreign visitors in the Amsterdam RAI Exhibition Centre on Tuesday 1 to Friday 4 November. For more information about the Horti Fair, please visit their website [www.hortifair.com](http://www.hortifair.com) or contact the Agricultural Department at Embassy of the Kingdom of the Netherlands in Kyiv (Tel. +380 44 4908223 or E-mail: [Kie-lnv@minbuza.nl](mailto:Kie-lnv@minbuza.nl)).

<sup>7</sup> This section has been drafted in cooperation with BEITEN BURKHARDT company (Turgenyevska, 38, Kyiv, 01054, Ukraine, [www.beitenburkhardt.com](http://www.beitenburkhardt.com)).

<sup>8</sup> Specific features of state adjustment of markets for agricultural goods and of land tenure are analyzed in UCAB studies "Largest Livestock Holdings of Ukraine: Development and Prospects", "Ukrainian Super-Large Farms: Facing Re-Structuring" and "Market Value of Arable Land in Ukraine" (2011).

- provision of credit subsidies;
- provision of budget subsidies to producers of animal products.

Measures of state support of agricultural producers include:

- allocation of budget subsidies in relation to a unit of cultivated area;
- partial budget compensation of cost of planted highly re-productive seeds of agricultural crops;
- realization of state programs for improvement of fertility of soil, elimination of pests and diseases of agricultural crops and animals, carrying out agricultural production in contaminated areas;
- organization of forward procurement of cereals on agrarian market;
- partial compensation of cost of construction or renovation of livestock farms and procurement of machinery for agricultural production;
- reduction of cost of means of identification and registration of animals; and
- compensation to agricultural producers of cost of construction of objects of social infrastructure in rural areas.

The state budget for 2011 does not provide for funding of all directions of state support to agriculture listed above. Measures actually funded in the current year are described below.

#### Reduction of credit costs for agricultural enterprises

Agro-industrial enterprises may count on partial compensation of interest rates on loans and borrowings in national and foreign currencies; the state budget for 2011 allocated for the purpose up to UAH 531.4 million. The procedure for use of the said money is provided for by the Resolution of the Cabinet of Ministers No. 794 of August 11, 2010 (with subsequent changes). This Resolution is limiting the compensation of interest rates by the following thresholds (higher rates are not compensated):

- no more than doubled NBU discount rate effective at the moment of interest rate calculation (for loans in national currency). Starting from August 2010, NBU discount rate has been set at the level of 7.75%; and
- no more than 10% on loans issued in foreign currency.

It is necessary to point out that compensation of interest rates on loans issued in 2007-2009 is performed regardless of effective interest rates, and only loans issued in 2010-2011 are supported within the limits described above.

Loans in respect of which state support is provided are qualified as follows:

- short-term (up to 12 months) issued in 2010–2011;
- mid-term (up to 36 months) issued in 2008–2011; and
- long-term (longer than 36 months) issued in 2007-2011.

Loans subject to state support also include those borrowings which were restructured in 2010.

When limiting the list of expenses incurred by agricultural producers (including farms belonging to educational establishments of agricultural profile) subject to support, the state defines the following types of beneficiaries:

- livestock and aviculture complexes;
- fisheries and fishing enterprises;
- sugar refineries;

- grain elevators and canneries;
- bakeries;
- state joint-stock company “Hlib Ukrayny” and its affiliates;
- agricultural wholesale marketplaces.

Resolution No. 794 is defining priority expenses subject to compensation; at that, support provided in 2011 in respect of loans issued in 2007 and 2010 may differ significantly.

Decision on compensation is taken by the commission of the Ministry of Agrarian Policy and Food of Ukraine, and preliminary selection of enterprises qualified for compensation is performed by tender commissions at regional level (in Oblasts, Autonomous Republic of Crimea, cities of Sevastopol and Kyiv).

It is necessary to mention that in recent years state budget has been allocating funds insufficiently for complete satisfaction of all submitted claims of agricultural producers.

#### Livestock subsidies

The state budget for 2011 provides for UAH 100 million for paying subsidies to farms producing livestock products. When this brochure was submitted for printing, there was no effective procedure for distribution of this sum in the current year (the procedure is subject to approval of the Cabinet). But respective resolution of the Government shall be expected soon. It is possible that large companies that have recently invested into vertically-integrated holdings will be eligible to the subsidy.

#### Partial compensation of cost of construction of new greenhouse complexes

State budget for 2011 provides for allocation of UAH 50 million for partial compensation of expenses incurred by agricultural producers when building new greenhouse complexes. As of today, there is no effective procedure for distribution of this subsidy.

#### Renovation of fixed assets of agricultural cooperatives

In 2011, there has been allocated UAH 5 million for support of agricultural cooperatives. The Cabinet approved procedure for use of this sum by its Resolution No. 272 of March 9, 2011. A coop that passed through a competition may claim compensation of up to 90% of value of machinery (VAT excl.) provided it has already paid at least 10% of the value to a supplier and concluded respective agreement with local department of agro-industrial development. This sum – UAH 5 million – is nothing serious at a regional scale, save for the national level, therefore it may concern technical re-equipment of only few coops.

#### Compensation of cost of agricultural machinery

The budget for 2011 has allocated UAH 10 million for this purpose (budgets of 2007 and 2008 provided for allocation of UAH 100 million and more). Resolution of the Cabinet of Ministers of Ukraine No. 647 of July 28, 2010 (with amendments) sets up the procedure for distribution of this sum and use thereof for partial compensation of expenses incurred in view of procurement of complex agricultural machines (of domestic origin). At that, the sum of compensation may cover up to 30% of the value of machinery (VAT excl.). Those entitled to compensation are chosen by special commissions on a competitive basis.



### Programs funded from a special fund of state budget

It is necessary to remember that the state budget for 2011 provided for allocation of financial support by the following directions: livestock subsidy (up to UAH 2.030 billion), support for planting of new gardens, vineyards and berry-fields (UAH 556.75 million) and also support for hop-growing (up to UAH 98.25 million).

By the end of April 2011, the Cabinet introduced changes into the procedure for calculation of VAT payable to state budget by processing enterprises. Respective Resolution (No. 523 of April 27, 2011) was published at official web-site of the Government.

Procedure sets up the mechanism for calculation of VAT payable to state budget by all processing enterprises (of all patterns of ownership); the tax is accumulated on a special account of the state budget. The procedure covers VAT accrued by processing enterprises when selling milk, dairy products, meat and meat products, other products from animals procured live weight (hides, offal and bone flour). The procedure is to be applied to VAT accrued starting from January 1, 2011 and till January 1, 2015. Resolution also prescribes how accumulated sums are used. It does not apply to toll processing of raw materials.



Budget funds are drawn according to the budgetary program “State Support to Livestock Sector” and directed for: paying subsidies on milk supplied to processing enterprises; partial compensation of cost of procured pedigree stock and cows of dairy, meat and combined breeds; interest rate on loans issued for funding of construction and renovation of livestock and aviculture farms and complexes, procurement of technological equipment and mechanisms, animals and poultry; cost of construction of feed plants; and cost of machinery for livestock sector and aviculture of domestic origin and equipment for individual milking. Sums of payments are defined on an annual basis according to respective allocations of the state budget.

Subsidy for milk is paid on a non-refundable basis to producers of milk (agricultural enterprises and natural persons) that produced and supplied milk to dairies, passed through attestation of production, per liter of milk, in terms of basis fatness. The subsidy is paid to producers by processing enterprises; in order to get compensated for paid sums, the latter shall submit a set of papers defined by Resolution No. 523 to the Ministry of

Agrarian Policy of Crimea or to Departments of Agro-Industrial Development of Oblasts, cities of Sevastopol or Kyiv.

Reimbursement of cost of cows procured by agricultural producers is done on a non-refundable basis and by results of a competition provided a producer procured from a nucleus (or imported) pedigree stock and cows of dairy, meat or combined breeds with weight over 350 kg from nucleuses (in 2011 – up to UAH 3 thousand per head).

Payment to enterprises of the agro-industrial complex of partial compensation of interest rates on loans issued for funding of construction and renovation of livestock and aviculture farms, procurement of technological equipment, animals and poultry is performed on a general basis according to the procedure provided for by the state budget.

Enterprises that have got compensation on account of funds of general fund of the state budget are not qualified for compensation on account of funds of special fund.

Payment to producers of partial compensation of cost of procured equipment and mechanisms (of domestic origin) for livestock sector and aviculture is performed on a non-refundable basis by results of a contest and may cover up to 30% of the cost incurred.

It is likely that state support for planting of new gardens, vineyards and berry-fields will not have much success as long as administration of special contribution for the purpose is still leaving much to be desired. In general, in view of the practice of collection and drawing of funds of special fund of the state budget, distribution of the said sums is questionable.

### 3.5. Effectiveness of agricultural production

Despite high risks typical for agricultural business, agriculture is still one of the most profitable business activities in Ukraine. In 2009, profitability of operating activities of agricultural enterprises accounted for 14.7% and exceeded even the indicator of mining of non-energy mineral deposits (which reported 11.3% profitability).

High attractiveness of agribusiness is additionally supported by information about the share of profitable farms in the sector. By results of 2010, over 80% of agricultural enterprises reported profitable<sup>9</sup> operations, and this is the best figure in the whole economy of Ukraine (see Figure 3.9). In the last five years the share of enterprises operating profitably in agriculture has never accounted for less than 68.7% (2006) i.e. at least 2/3 of agricultural enterprises were profitable.

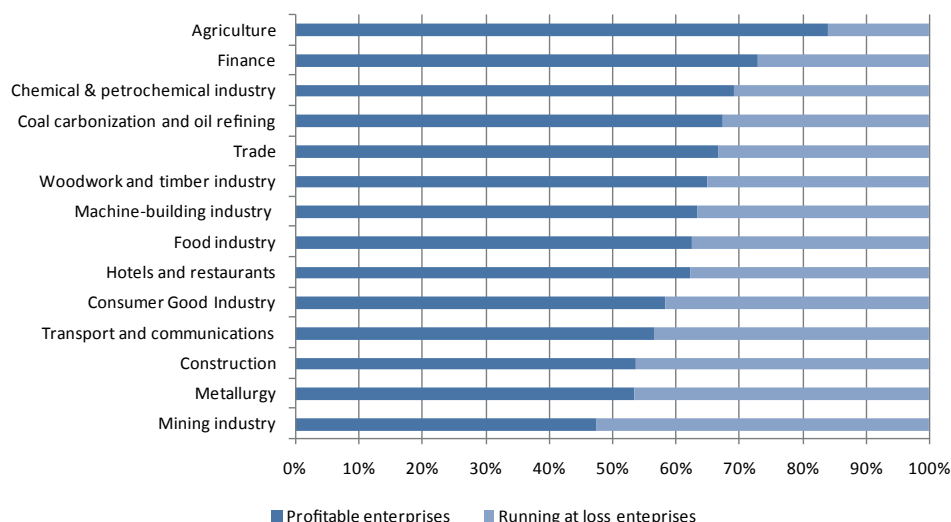
If taken by sectors, it is clear that crop growing is showing better results than others, its profitability in recent years varied from 10 to 30% (see Figure 3.10). Main drivers behind these figures are fertile black soils of Ukraine, moderate continental climate, low level of wages and availability of sea trade ports with necessary infrastructure. The livestock sector has managed to reach break-even operations only in the last couple of years, and only in respect of some kinds of output.

Low productivity of animals, poor working efficiency, conversion of feed and quality of output are all reasons making Ukrainian animal products insufficiently competitive and unprofitable.

<sup>9</sup> Profitability is assessed on the basis of financial result of regular activities taken before taxation.

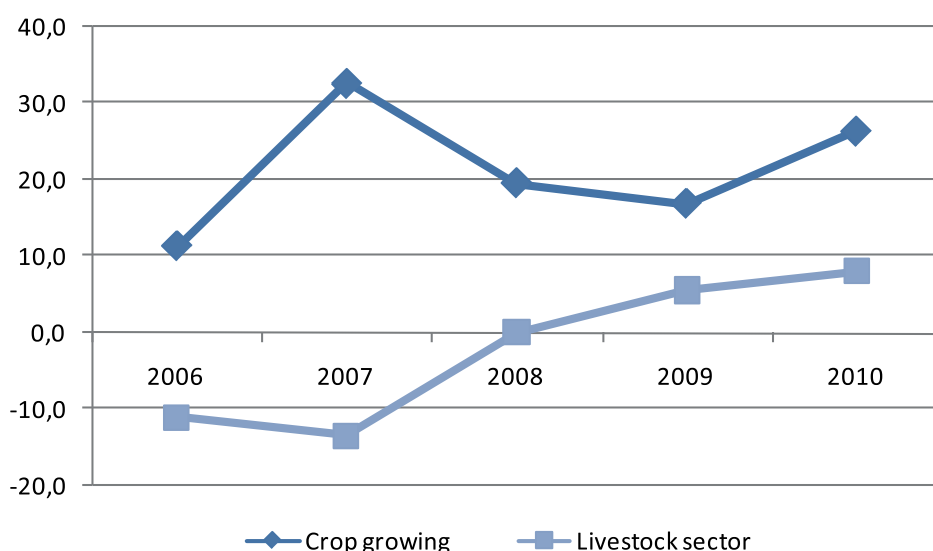
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**Figure 3. 9. Share of profitable and unprofitable (running at a loss) enterprises by types of economic activities in 2010**

Source: State Statistics Committee



**Figure 3.10. Dynamics of profitability<sup>10</sup> of crop growing and cattle breeding reported by agr. enterprises in the last 5 years, %**

Source: State Statistics Committee

<sup>10</sup> Here and elsewhere in this section "profitability" means percent ratio of difference between earnings from sales (crops/animal products, VAT and subsidies excl.) and full cost of sold output.

If we look at efficiency of cultivation of different crops (see Figure 3.11), it becomes clear why Ukraine is enhancing production of cereals and oil crops and maintaining top positions in global ratings of exporters of grain, rape seed, sunflower oil and sunflower seed.

As we may see, top profitability (though very volatile) in the last five years has been reported in respect of sunflower; the level of profitability of rape cultivation is also quite high and much more stable as compared to sunflower; efficiency of cultivation of cereals is somewhat lower than that of oil crops but it is still enough attractive to stimulate further growth of production. Efficiency of growing sugar beet depends to a large extent on state support and the level of coverage of domestic consumption of sugar on account of local production.

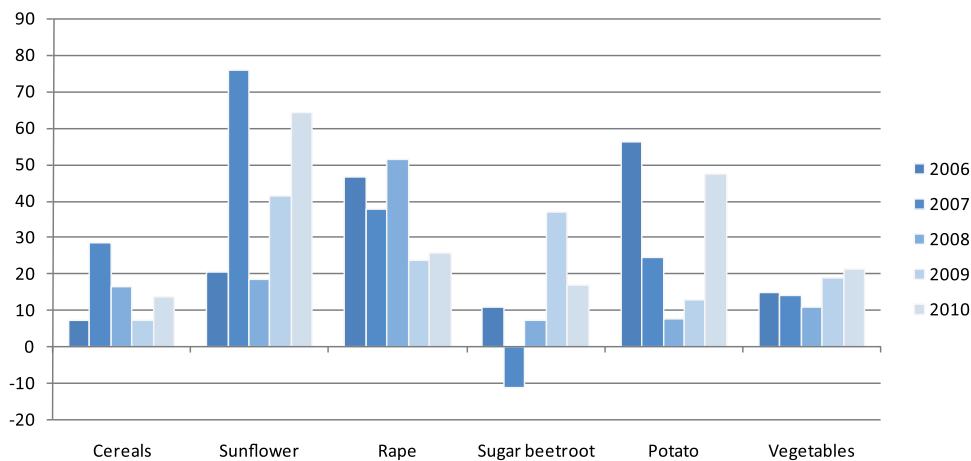


Figure 3.11. Profitability of crop growing at agricultural enterprises of Ukraine, %

Source: State Statistics Committee

Production of potato and vegetables is not a priority for agricultural enterprises due to high capital intensity of production and monopolization of production by households. Moreover, there is a clear and acute lack of necessary infrastructure (storage and realization); it is also true that export potential is limited. Nevertheless, those agricultural enterprises that engaged in cultivation of potato and vegetables are showing fairly good profitability.

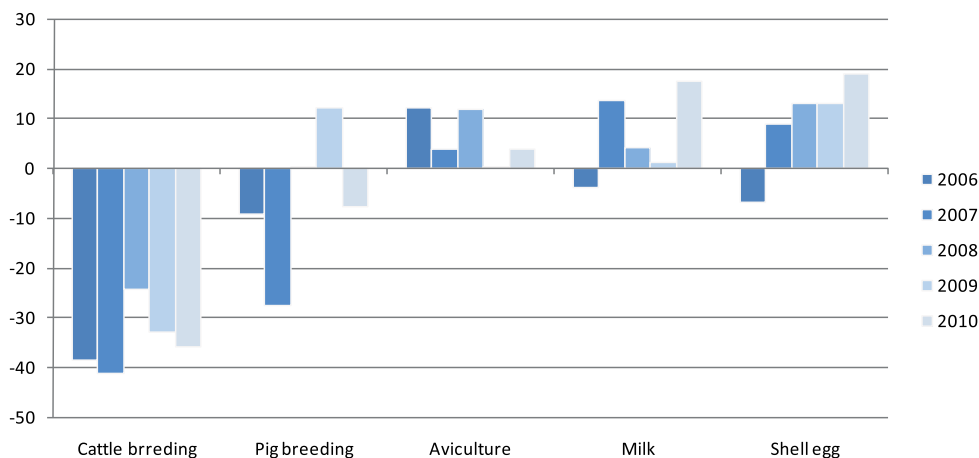


Figure 3.12. Profitability of livestock breeding at agricultural enterprises of Ukraine, %

Source: State Statistics Committee

As we may see in Figure 3.12, efficiency of production of main types of animal products in Ukraine is quite poor. The only exception is made by aviculture (poultry meat and eggs) where production is concentrated mostly on farms employing high technologies.

Production of milk due to a deficit of milk on the Ukrainian market reported certain profitability but, due to inseparability of efficient dairy production with inefficient raising of young cattle, the overall result of dairy farms is mostly negative.

Poor genetics of pigs, imbalanced feed, low efficiency of labour are key drawbacks of Ukrainian pig breeding sector which, combined with deterioration of prices for pigs on the domestic market, have driven the sector back at running at a loss. Only few farms, employing the most advanced technologies, look into the future with confidence.

### 3.6. Brands of input markets

«Ukrainian Agribusiness Club» (UCAB) and Kyiv International Contract Fair hold the annual contest “AgroBrand”; the contest is aiming at shaping and development of awareness of trademarks, provision of unbiased appraisal of effectiveness of marketing policy of companies supplying inputs for agricultural production, studying of market dynamics and changes in requirements of consumers (agricultural producers). Based on the results of the contest, best suppliers of resources are defined and awarded. There are following nominations: «Best supplier of agricultural machinery”, “Best supplier of agrochemicals”, “Best producer of agricultural crop seeds” and “Best dealer of agricultural inputs”. Ranking of nominees is performed through phone interviews of managers, chief agronomists and chief engineers of agricultural enterprises. The sampling error at interviewing of 1000 respondents does not exceed  $\pm 3\%$ . Besides expediency (annual contest) and representativeness, principles of the contests are objectiveness and openness; control is done at every stage of data collection, representatives of media, business and experts are invited. Unprejudiced attitude of organizers is beyond doubts.

There have been interviewed 1129 agricultural producers within the framework of this year “AgroBrand” contest. Results of the contest are pointing at domination of international trademarks on the Ukrainian market, despite competition on the part of domestic suppliers and producers. The results of contest proved that John Deere is the most recognizable and well-known brand of agricultural machinery (39% of respondents referred to this brand). The second position was occupied by Minsk Tractor Works, MTZ (29%) and the third by Claas (16%).

Leadership in nomination “Best producer of agricultural crop seeds” was awarded to Pioneer (27%) followed by Syngenta (20%) and Gardens of Ukraine (11%).

Serious competition was observed in the nomination “Best supplier of agrochemicals” where Bayer and Syngenta contested the status of the most recognizable brand with 27% and 25% votes respectively. The third place in the nomination was awarded to BASF (7%).

RISE won the leadership in the field of input supply (34%) while the second and the third positions in the nomination were taken by Eridon (21%) and AMAKO (9%).



Table 3.5. Winners and awardees of “AgroBrand-2011” contest

Winners	Awardees
<b>Best supplier of agricultural machinery</b>	
JOHN DEERE	MTZ
	CLAAS
<b>Best supplier of agrochemicals</b>	
Bayer CropScience	SYNGENTA
	BASF
<b>Best producer of agricultural crop seed</b>	
PIONEER	SYNGENTA
	Gardens of Ukraine
<b>Best dealer of agricultural inputs</b>	
Rise	Eridon
	AMAKO

## 4. Farmland market of Ukraine

### 4.1. Land tenure in Ukraine

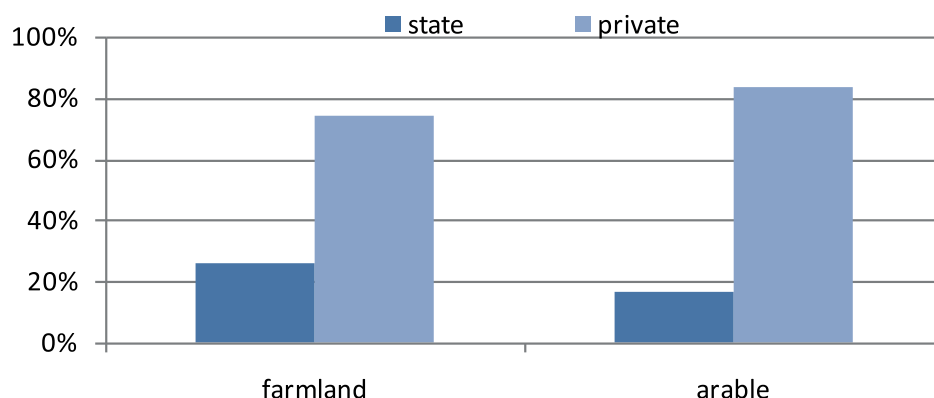
Ukraine is one of a few countries having rich fertile land resources. About 69% of the national land stock is suitable for agriculture; over half of 60 million ha of the total national area is qualified as arable land. Over the last decade, there has been no material change in distribution of land resources between different categories, and it is unlikely that such change will take place in the nearest future. It is possible that part of land qualified as “agricultural” was in fact bought for non-agricultural purposes and is not currently used in agricultural production; this is especially true in respect of areas bordering large cities and infrastructural objects. Formalization of these transactions may reduce the total area of land currently attributed to the category of agricultural land.

Table 4.1. Structure of farmland of Ukraine as of January 1, 2011 (thousand ha)

Total national area	60354,8
Agricultural land, total area	41576,0
Including	
arable land	32476,5
fallow land	310,2
perennial plantations	896,5
hay-fields	2410,9
pastures	5481,9

Source: State Agency of Land Resources

Upon completion of the first stage of land reform in the mid-90ies of the last century, private ownership became a dominant pattern of land ownership in the country. It is particularly noticeable in respect of farmland, of which 74% is privately owned; the share of privately owned arable land is even higher and accounts for 83%. Upon lifting of the moratorium and introduction of full-fledged land market, the share of private owners in the general structure of ownership of land resources may further increase, partly due to sale of some public farmland.



**Figure 4.1. Structure of farmland ownership, 2010**

Source: State Agency of Land Resources

Despite attempts to bed in the traditions of farmership in Ukraine, agricultural enterprises are still the main land users in agriculture. The share of arable land in cultivation of enterprises accounts for 47.5% while farmers managed to accumulate 11.8% thereof. Rural households are also among large agricultural land users, they hold about a third of all arable land in the country. We do not foresee remarkable changes in the structure of land use in the nearest future (see Table 4.2); only slight redistribution in favour of agricultural enterprises may be expected.

**Table 4.2. Use of farmland as of January 1, 2011  
(thousand ha)**

	Agricultural land	incl.arable land
<b>In total</b>	<b>41576,0</b>	<b>32476,5</b>
<b>Including in use of</b>		
<b>Citizens (households)</b>	<b>15898,3</b>	<b>11694,7</b>
<b>Agricultural enterprises</b>	<b>16577,2</b>	<b>15412,8</b>
<b>Farmers</b>	<b>4012,4</b>	<b>3824,6</b>

Source: State Agency of Land Resources

As of the beginning of the current year, 59% of all arable land in Ukraine was leased out; about 80% of that land is represented by so-called land shares (pai) owned by rural dwellers as a result of privatization of landholdings of collective agricultural enterprises. Evaluation of the influence which current structure of land ownership may have upon expected farmland market is presented in UCAB study “Market Value of Arable Land in Ukraine”.

This year, just like year before, the largest areas of farmland are used for cultivation of cereals and leguminous crops (see Figure 4.2). The second – in terms of cultivated area – crop is sunflower upon which 11% of cultivated area is falling. Potato is traditionally planted at 5% of farmland. The dark horse of the last decade – rape seed – has maintained the same area under crop (4%); despite attractive economy of rape growing, weather conditions during the past two sowing seasons prevented further expansion of areas under winter rape. The areas under soya have been steadily growing in recent years. Despite 10% expansion of areas under sugar beet, it is still occupying about 2% in the overall structure of cultivated areas.

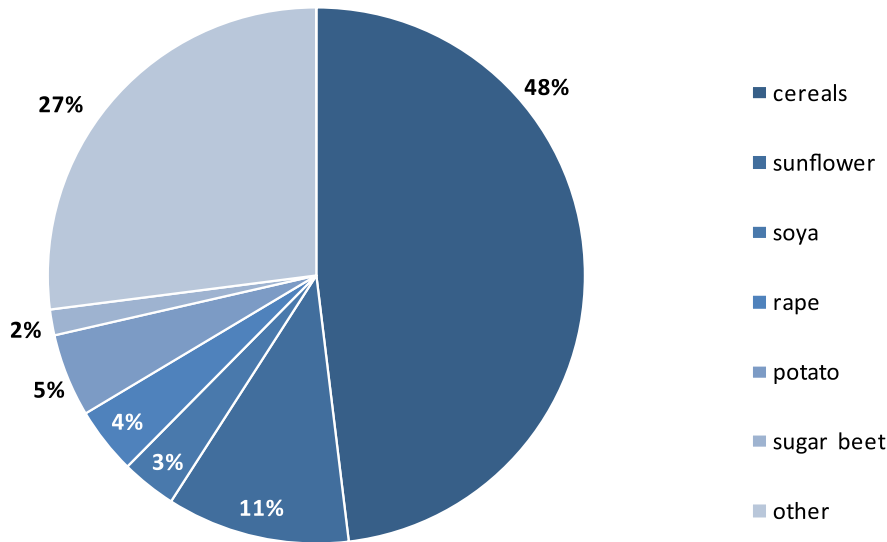


Figure 4.2. Structure of areas under agricultural crops (according to the Ministry of Agrarian Policy and Food, as of May 2011)

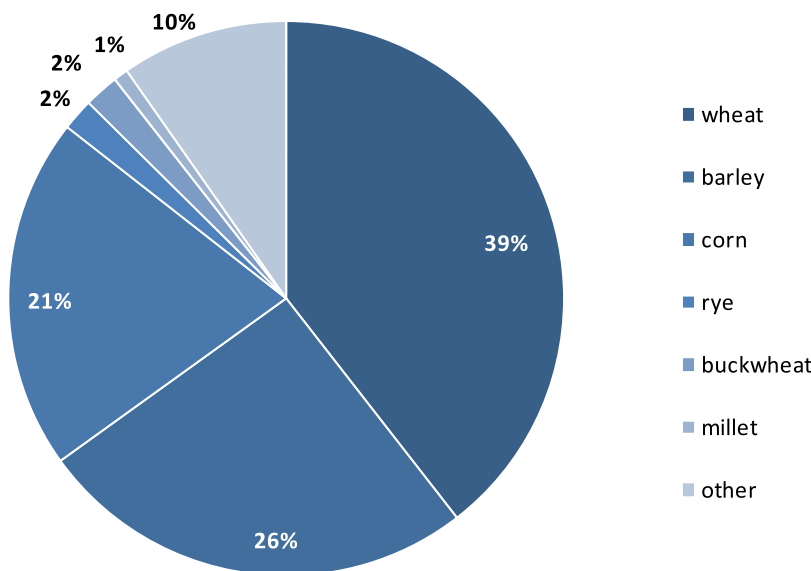


Figure 4.3. Structure of areas under cereals and leguminous crops (according to the Ministry of Agrarian Policy and Food, as of May 2011)

In general, the structure of areas under crops which emerged in the last five years has not undergone any significant changes in the current year.

Expected strengthening of state control over crop rotations may lead to reduction of areas under crops which exhaust the soil, namely, under sunflower and rape. Another possible effect of more stringent control over rotations may be distortion of public reports on use of farmland.

#### 4.2. State adjustment of land market<sup>11</sup>

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Upon declaration of independence of Ukraine, land reform became one of the most important reforms in the country. The reform has practically eliminated state and collective ownership to arable land. Today virtually all farmland is owned by former members and employees of kolkhozes and sovkhoses and

<sup>11</sup> This section has been drafted by BEITEN BURKHARDT company (Turgenevska street 38, Kyiv, 01054, Ukraine, www.beitenburkhardt.com).

their heirs. It is necessary to note that land reform took the fast track, but it has remained incomplete.

It is important to understand that a land share (pai) is not identical to a land parcel; a land share is only a right to be allocated a piece of land of a certain area. Conversion of land shares into real land parcels with registered ownership is currently going on, but not every owner has already completed necessary procedures, and that often brings about conflicts and disputes. Significant areas of farmland in the beginning of 90ies were divided among former employees of kolkhozes, and nowadays about 40% of farmland is owned by people who have nothing to do with agriculture. The situation is further complicated due to incomplete legal regulation of issues of succession in case of land shares.

Most citizens who became landowners in the course of land reform were not prepared to farm their land; they were also reluctant to make any associations for joint cultivation of their plots.

Therefore, in most cases, farmland is cultivated by enterprises that lease land (parcels or land shares) from citizens. In some cases, tenants are foreign investors.

Establishment of a farmland market is one of the principal directions of economic reforms announced by the President of Ukraine and the Government.

The moratorium on sale of farmland has been a notorious feature of Ukrainian land market of the last decade. According to the current reading of the law on moratorium, the latter shall be lifted with adoption and entering into force of two laws, "On land market" and "On land cadastre", but not earlier than January 1, 2012. At the moment the law "On land cadastre" was upheld by the Parliament of Ukraine in the first reading; and the law "On land market", while being actively debated by experts and public at large, has not been submitted to the scrutiny of the Parliament yet.

Expectations on a lifting of the moratorium in the nearest future are also supported by statements of high ranking officials and Deputies belonging to the ruling Party of Regions.

Draft law of Ukraine "On land market" (at least, its reading which became public at the end of April 2011) provides for several restrictions related to farmland ownership. The draft, similar to effective Land Code of Ukraine, explicitly forbids foreign companies as well as joint ventures and foreign citizens to own farmland in Ukraine. Besides, it appears that only citizens of Ukraine, according to the draft, will be allowed to own farmland, and any corporate landownership will be banned. Land market is going to be actively regulated through specialized state establishment.

At the same time, the rule limiting the list of potential owners of farmland by citizens of Ukraine is not clear enough and may give rise to ambiguity and inconsistency. The draft says that only those citizens of Ukraine are entitled to own farmland who possess agricultural education or carry out agricultural commodity production. However, the draft does not specify how these facts shall be confirmed or checked. But the keynote of the draft is clear: to protect Ukrainian farmland from being acquired by foreigners in order to ensure food security of Ukraine.

The draft also provides for a limit on the area of farmland to be owned by one person. Initially, it was thought that respective limits would be defined

by the Cabinet on the basis of availability of land in different regions. After numerous submissions to drafters, this rule was changed, and currently upper limits are in the text of the draft.

Maximum area of farmland to be owned by one person is defined in relation of so-called natural agricultural zones (mountain areas) and equals to:

- Polissya (Forest) - 1500 ha;
- Forest Steppe – 1750 ha;
- Steppe, Arid Steppe, Dry Steppe – 2100 ha;
- Carpathian Mountain Oblast – 900 ha;
- Crimean Mountain Oblast – 1100 ha.

However, this approach also leaves questions; for example, it is unclear whether one person may own maximum areas in every zone or a maximum area for one zone shall be understood as absolute limit on area of farmland in hands of one citizen. Besides, the boundaries of the said zones are not defined in law, therefore the rule leaves enough space for abuse and confusion on the market.

Another issue of top importance for agricultural producers is the pre-emption right provided for by the draft. Currently effective laws establish such right for tenants, and most agricultural enterprises are tenants, not owners of the land they cultivate. Draft, upon testing different variants, was amended with the rule providing for the first pre-emption right of the state specialized establishment to be set up by the Cabinet of Ministers of Ukraine.

The second pre-emption right (if the first right is waived) is attributed to local communities, i.e. in fact to local – village, town, city – councils (Radas).

The third right – if the second right is waived – may be realized by current user (tenant) of land parcel, and the fourth right is given to owners of adjacent plots (neighbours). Pre-emption right tool is not triggered if land is sold to members of owner's family.

The draft also defines how the owner of a land plot who is willing to dispose of his land informs potential buyers and holders of their pre-emption right. The owner shall inform holders of the first and the second rights and publish in local press an advertisement specifying the price of land.

Therefore, the land owner is exposed to additional expenses: of time (the draft provides for a period during which holders of the pre-emption right shall take decision on discharge or waiver of their right) and of money, as soon as publication is on his account. Besides, this rule brings about many questions and may well lead to disputes.

Restrictions embodied in the draft are most likely called upon to prevent accumulation of Ukrainian farmland in hands of few persons; nevertheless, the danger of such accumulation shall be balanced against another danger, namely, technological and financial cast down of Ukrainian agriculture to the bottom of the national economy.

Open and predictable farmland market shall support development of agriculture of Ukraine and attract investors, though the latter may have limited options. It is possible that variations of leasehold will become the last ditch for foreign investments. We expect that the moratorium on sale of farmland will be lifted, but, most likely, starting only from January 1, 2013.



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### 4.3. Key players of the land market<sup>12</sup>

Recently, representatives of different levels of public administration as well as politicians have signaled the necessity of expedient introduction of farmland market (in 2012). Based first of all on understanding of the potential market value of land, it is interesting to analyze possible behavior and influence of key players of the land market.

#### State

Despite its status of the largest landowner, the state has until recently played a limited role on land lease market. It is obvious that strengthening of its role before lifting of the moratorium is inevitable. At that, it is necessary to distinguish the role of the state as a market regulator and as a landowner and market player. The last available reading of the draft law "On land market" allows for a conclusion that these roles of the state are going to be closely intertwined (see sub-section 4.2).

#### Agricultural enterprises

The role of enterprises will to a large extent be defined by the decision taken on corporate land ownership.

In case corporate land ownership is admitted and legally allowed, the situation will become predictable. Every enterprise will set up a certain price ceiling based on actual economic results of land use, quality of soil, availability and cost of financial resources and position of owners of land shares.

The situation will become less clear if corporate land ownership is banned. Then there could be several scenarios which will depend on corporate decisions and strategies:

1. Acquisition of land in the name of natural persons being owners and/or relatives of owners of enterprises. This approach will demand preliminary legalization of funds.
2. Acquisition of land in the name of third natural persons with simultaneous burdening them with some financial obligations.
3. Initiation of long-term lease agreements securing the right to cultivate land for a considerable period of time.
4. Conclusion of contracts for purchase of land with payment by installments in view of possible liberalization of legal regime of farmland.

Thus, agricultural enterprises will have some space for maneuvering on land market even if the draft becomes a law in its current wording.

#### Agrarian holdings

<sup>12</sup> Detailed analysis of behavior of key players is presented in UCAB study "Market Value of Arable Land in Ukraine" (2011).

Options of holdings are in general similar to those of enterprises, but with adjustment to scale of business. For example, owners of holdings will unlikely be able to purchase the land they currently cultivate in the name of their relatives in view of modest limits on area of land to be owned by one person. Many holdings will have to operate with the rate of ground rent in order to win competition over land. One may assume that competition between holdings and average agricultural enterprises on the land lease market will be transferred to land sales market, and holdings will be offering higher prices. However, if corporate land ownership is banned, rates of rent will unlikely be influenced by lifting of the moratorium.

#### Farmers

Interests of farmers are clear. Most farmers (except for several tenths which are farmers only in formal terms but in fact already turned into typical enterprises or even small holdings) are family businesses, and they will be able to secure their land use by purchasing land in the names of family members.

In contrast to other legal entities often owned by several persons, farmers will have no difficulties in securing loans with their land. That is, factors limiting crediting upon land pledge may be easily bypassed.

Farmers are often owners of land shares appended to their farms and, therefore, they will also have pre-emption rights, though only of the fourth turn (in fact, in third, as soon as corporate land ownership is banned).

Therefore, current wording of the draft law on land market is mostly suited to farmers.

#### Private investors

Natural persons having nothing to do with agricultural production would have slim chances to establish themselves on the land market if corporate land ownership was allowed. However, expected restriction on corporate ownership is creating an opportunity for such investors, and many of them are already estimating their chances of making good profit on arable land market in view of initially low prices. Besides financial investors, managers of agrarian companies and persons associated with local authorities are to be found among those going to play on the land market.

#### Owners of land shares

As a result of land reform, 27.72 million ha of farmland were transferred into private ownership (so-called land shares, *pai*). Land shares were divided and distributed among 6.91 million citizens, and every person at average got about 4 ha of arable land. Today land shares are used like follows: 17.4 million ha is leased out to agricultural producers (63%); 1.15 million landowners preferred to get their 4.4 million ha (16%) allocated in kind and farm them themselves; about the same number of landowners – 1.17 million – are still undecided about 4.07 million ha. Approximately 342 thousand ha of arable land is still qualified as “unclaimed land shares”.

In view of the figures stated above, we would assume that the potential offer of arable land at the initial stage of land market functioning (3-5 years) may exceed 6 million ha. Detailed analysis of supply and demand sides by forms of land use is presented in UCAB study “Market Value of Arable Land in Ukraine”.



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#### 4.4. Possible Market Value of Farmland

As it has been already stated, the probability of farmland market opening in the nearest year or two is getting higher. However, besides tackling of legislative and organizational issues, the cornerstone of a future land market at the initial stage of operation is the question of actual land value.

There are two main approaches for calculation of land value employed in the world:

- income approach (method of capitalization of income);
- comparative approach (method of value comparison).

As long as sale of arable land in Ukraine is formally prohibited, income method is nearly the only tool available for trustworthy estimation of hypothetical land value. We believe that at the initial stage of market functioning a considerably large number of buyers will be calculating land value based on the number of years necessary for recovering investments made into purchase of land. Many alternative investments are often showing recovery term of 5-7 years; therefore, in the context of farmland, its price will be estimated on the basis of the same terms.

Just like on any other market, besides price offers of buyers there will be price offers of sellers, i.e. of owners of land shares. We believe that sellers will be mostly motivated by two main factors:

1. Conditionally rational considerations, i.e. when decisions on sale of land are based upon comparison of income accrued from lease and from sale. Rationality in this instance will be conditional, as long as hardly anyone will be discounting cash flow. It will look quite simple; for example, landowners will favorably accept the price which will make up 10, 20 or 30 annual rents.
2. Emotional attitudes. Vision of land price may be shaped by information about land prices in other countries. This approach allows for unlimited freedom of imagination; for example, rural dwellers were informed that “just” land price would be at the level of USD 10 thousand per ha.

Estimates and suggestions of UCAB allow for placing possible farmland price into the range from UAH 5 thousand to UAH 12 thousand. Detailed analysis of farmland market value is available in the UCAB study “Market Value of Arable Land in Ukraine”. The study also gives account of regional factors of pricing, presents results of questioning of agricultural producers about potential land value and readiness to sell or to buy farmland.







## 5. About UCAB

### 5.1. General information

Association “Ukrainian Agribusiness Club” (UCAB) is a non-governmental organization representing interests of large and medium agrarian business and acting on its behalf. Effective promotion and lobbying of interests of UCAB members is ensured by defining overall priorities of agrarian business, debating drafts of the most important laws and by-laws, supporting members in tackling current issues, establishing and maintaining close and fruitful relations with the authorities of Ukraine, foreign states, embassies and international organizations. The UCAB mission is enhancement of effectiveness of the agricultural sector through improvement of business environment, attraction of investments and technological re-equipment.

The team of UCAB consists of highly qualified experts who have managed in only a few years of dynamic work (since September 2007) to implement successfully a number of projects aiming at improvement of business conditions for UCAB members and the whole sector.

Due to the credibility of our experts, UCAB nowadays is the most often quoted association of the agro-industrial complex of Ukraine, equally by print and electronic mass media.

The Association possesses the complete range of effective tools for attaining its goals, in particular, it provides reliable analytics, maintains regular correspondence with the authorities of Ukraine, promotes institutionalization of collaboration of business and public administration, organizes and holds conferences, roundtables and workshops, undertakes media campaigns, develops and implements projects aiming at realization of UCAB mission.





UCAB always sustains direct contact with owners and top managers of leading companies. The Association today is a union of persons sharing common views upon development and advance of agro-industrial complex of Ukraine.

#### Members of Association

UCAB membership opens for agrarian companies the full access to all necessary services provided by the Association.

Members and partners of the Association are the largest agro-industrial companies that have already become trademarks of agrarian Ukraine and confidently striving towards global leadership. Members of UCAB are active in crop growing, the livestock sector, dairy and meat processing, cultivation of vegetables and production of sugar. These companies are jointly farming over 4 million ha and employing over 100 thousand workers in agriculture and food industry. Some largest transnational companies – producers of agricultural equipment, seeds, chemicals etc. – are also among the members of UCAB.

## 5.2. Our team



	<p><b>Alex Lissitsa</b> President lissitsa@agribusiness.kiev.ua</p>	<p>Acknowledged leading expert in the field of strategic and operational management, analysis of productivity and efficiency of enterprises in agriculture and food industry</p>
	<p><b>Heinz Strubenhoff</b> Advisor to President strubenhoff@ier.kiev.ua</p>	<p><b>AgroInvest</b> Consulting on funding, organization of technical and operational due diligence, development of business models, advising on potential investments, banking, legal and auditing partners, system support in entering Ukrainian and international stock exchanges.</p>
	<p><b>Volodymyr Lapa</b> Director General lapa@agribusiness.kiev.ua</p>	<p><b>AgroInvest</b> Consulting on funding, organization of technical and operational due diligence, development of business models, advising on potential investments, banking, legal and auditing partners, system support in entering Ukrainian and international stock exchanges.</p>
	<p><b>Karen Fisher</b> Deputy Director General, Coordinator of International Relations fisher@agribusiness.kiev.ua</p>	<p><b>AgriLink</b> Establishment of links between Ukrainian and foreign companies. Provision of services, information support, knowledge transfer, establishment and maintenance of contacts, coordination of collaboration with international partners. Initiation and implementation of joint projects with partners and clients.</p>

	<p><b>Elizaveta Svyatkivska</b> Executive Director, Expert on Market of Meat and Meat Products liza@agribusiness.kiev.ua</p>	<p>Expert in the field of production and processing of beef, pork and poultry.</p>
	<p><b>Roman Slastyon</b> Director of “AgriEfficiency” Agency www.agriefficiency.kiev.ua info@agriefficiency.com.ua</p>	<p><b>AgriEfficiency</b> Detailed comparative analysis of productivity and efficiency of farms at national and international level. Detection of strengths and weaknesses of organization of production, analysis of efficiency of production process.</p>
	<p><b>Anatoliy Tsyrukun</b> Director of “AgriEvent” Agency www.agrievent.com.ua info@agrievent.com.ua</p>	<p><b>AgriEvent</b> Complex professional event management for business, corporate and private clients. Selection of premises, translation services, technical support, catering, transport services and other related services</p>
	<p><b>Khrystyna Protsiv</b> Director of “AgriPR” agency, head of department for cooperation with media press@agribusiness.kiev.ua</p>	<p><b>AgriPR</b> Broad range of services in the field of establishing public relations for agrarian companies (lobbying, marketing, corporate and crisis PR). Selection of appropriate methods of communications with target audience for ensuring best results</p>
	<p><b>Eleanora Evchenko</b> Director of “AgriJob” Agency www.agrijob.com.ua resume@agrijob.com.ua</p>	<p><b>AgriJob</b> Leading recruiter of personnel for the agrifood sector. Provision of high quality services in the field of personnel selection for local and foreign companies. Selection of managers, headhunting, direct search for staff, maintenance of a database of employers and potential candidates.</p>

	<p><b>Taras Gagalyuk</b> Director of “AgriSurvey” Agency info@agrisurvey.com.ua</p>	<p><b>AgriSurvey</b> Complete range of marketing studies for key players of agrarian sector. Provision of reliable data for taking strategic decisions, for better understanding of business environment and distinguishing drawbacks and strong sides of business.</p> <p><b>AgroBrand</b> Survey of visibility of trademarks and brands among agricultural producers. Annual awarding of most successful brands of resource companies.</p>
	<p><b>Inna Iliencko</b> Coordinator of “AgriBenchmark” project in Ukraine and Russia. Expert of agrarian markets (milk and dairy) ilienko@agribusiness.kiev.ua</p>	<p><b>AgriBenchmark</b> International comparative analysis of productivity and efficiency of production of agricultural output. Detection of inefficient use of resources, improvement of efficiency of business, reduction of unproductive costs, analysis of competitiveness of Ukrainian producers at global scale.</p>
	<p><b>Taras Vysotskyi</b> Expert of agrarian markets vysotskyi@agribusiness.kiev.ua</p>	<p>Expert in the field of sugar refining industry of Ukraine, efficiency and productivity of agriculture.</p>
	<p><b>Oleksandr Verzhovskiy</b> Expert on quality and safety of agricultural products verzh@agribusiness.kiev.ua</p>	<p><b>AgriCert</b> Analysis of situation in the field of certification of agricultural products, quality and safety of foodstuffs.</p> <p><b>AgriFYI</b> Monthly electronic newsletter offering information on current situation in the agri food sector of Ukraine. Exclusive information, news of agriculture, papers, statistics etc.</p>

	<p><b>Tetiana Varchenko</b> Coordinator of relations with governmental bodies varchenko@agribusiness.kiev.ua</p>	<p><b>AgriLobby</b> Cooperation with authorities at national and local level. Participation in development and promotion of state programs and projects, state standards in the field of agriculture, in analysis of draft law and by-laws etc.</p>
	<p><b>Galyna Romanchuk</b> Chief Accountant romanchuk@agribusiness.kiev.ua</p>	<p>Accountant with extensive experience in Ukrainian and international organizations.</p>
	<p><b>Kateryna Stetsko</b> Accountant stetsko@agribusiness.kiev.ua</p>	<p>Specialist in the field of accounting and auditing</p>
	<p><b>Oksana Artemchuk</b> Assistant to the President info@agribusiness.kiev.ua</p>	<p>Organizational and technical support for functioning of UCAB office.</p>
	<p><b>Marina Popova</b> Account Manager info@agrijob.com.ua</p>	<p>Research of labour market, professional and psychological testing.</p>
	<p><b>Maksym Lapa</b> Project Manager m.lapa@agribusiness.kiev.ua</p>	<p>Moderation of UCAB internet-based resources, organizational tasks</p>



	<p><b>Sergey Khaletsky</b> IT department, Project Manager khaletskii@agribusiness.kiev.ua</p>	<p>Administration of internet-based resources of UCAB, web-designing, programming, support to working stations and users.</p>
	<p><b>Vitalii Lanovliuk</b> Project Manager lanovliuk@agrievent.com.ua</p>	<p>Event management: conferences, trainings, business-forums, other events.</p>

### 5.3. UCAB studies of 2011

UCAB offers studies of the following categories:

1. Marketing studies (surveys)
2. Multi-client studies
3. Studies for UCAB members (price monitoring and reports. These as well as all other studies are provided to members under special conditions)
4. Economic studies (economic modeling, analysis of international trade, markets, etc.)

Title	Cat	Language	Date of issue
Largest livestock holdings in Ukraine: development and perspectives	2	Russian/English	15/03/2011 (in Russian), 30/03/2011 (in English)
Agri-food spectrum of Ukraine: personal profile	2	Ukrainian/English	20/03/2011 (in Ukrainian), 31/03/2011 (in English)
Market Value of Arable Land in Ukraine	2	Russian/English	10/05/2011 (in Russian), 30/04/2011 (in English)
Doing Agribusiness in Ukraine 2011	2	Russian/English	25/05/2011
Meat Market: Production, Trade, Potential	4	Russian/English	15/05/2011
Largest Agricultural Companies of Ukraine: On the Verge of Restructuring	2	Russian/English	15/08/2011 (in Russian), 31/08/2011 (in English)
Analysis of Demand of Agricultural Producers for Agricultural Equipment	1	Ukrainian/English	12/09/2011
Attitude of Agricultural Producers Towards Genetically-Modified Seeds	1	Ukrainian/English	12/09/2011
Production and Processing of Milk	4	Ukrainian/English	01/11/2011
Meat Market Monitor	3	Russian	Monthly
AgriFYI (monthly UCAB bulletin plus quarterly report on machinery)	3	Russian	Monthly

#### Contacts:

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<http://www.agribusiness.kiev.ua/uk/service/studies/>

## 6. List of Useful Contacts

Name	Contact
Ministry of Agrarian Policy and Food of Ukraine	Address: 24 Khreshchatyk, Kyiv, 01001, Ukraine Tel.: +380 44 279 8474; +380 44 279 8474 <a href="http://www.minagro.gov.ua">http://www.minagro.gov.ua</a>
Ministry of Economic Development and Trade of Ukraine	Address: 12/2 Grushevskogo str, Kyiv, 01008, Ukraine Tel.: +380 44 253-9394; fax: +380 44 226 3181 <a href="mailto:meconomy@me.gov.ua">meconomy@me.gov.ua</a> ; <a href="http://www.me.gov.ua">http://www.me.gov.ua</a>
State Statistics Committee of Ukraine	Address: 3 Shota Rustaveli str., Kyiv, 01023 MPS, Ukraine Tel.: +380 44 287 2433; fax +380 44 235 3739 <a href="mailto:office@ukrstat.gov.ua">office@ukrstat.gov.ua</a> ; <a href="http://www.ukrstat.gov.ua">http://www.ukrstat.gov.ua</a>
State Veterinary and Phyto-Sanitary Service of Ukraine	Address: 1 B. Grinchenko str., Kyiv, 01001, Ukraine Tel.: +380 44 279 1270; +380 44 279 4883 <a href="http://vet.gov.ua">http://vet.gov.ua</a>
State Agency on Land Resources of Ukraine	Address: 3 narodnogo Opolchennya str., Kyiv, 030151, Ukraine Phone: +380 44 2499691, fax +380 44 2499670 <a href="mailto:dkzr@dkzr.gov.ua">dkzr@dkzr.gov.ua</a> , <a href="http://dkzr.gov.ua">http://dkzr.gov.ua</a>
Institute for Economic Research and Policy Consulting	Address: 8/5-A Reytarska str., Kyiv, 01034 Phone: +380 44 278 6342; 278 6360, Fax: +380 44 278 6336 <a href="http://www.ier.kiev.ua">http://www.ier.kiev.ua</a>
German-Ukrainian Policy Dialogue in Agriculture	Phone: +380 44 2539394, fax +380 44 22633181
National University of Life and Environmental Sciences of Ukraine	Address: 15 Geroyiv Oborony str., Kyiv, 03041, Ukraine Phone: +380 44 527 8233 <a href="mailto:rektorat@nauu.kiev.ua">rektorat@nauu.kiev.ua</a> , <a href="http://nubip.edu.ua">http://nubip.edu.ua</a>
Ukrainian Laboratory of Quality and Safety of Agricultural Products	Address: 7 Mashinobudivelna str., Chabany village of Kiev Oblast Tel./fax: +380 44 5264504 <a href="mailto:info@quality.ua">info@quality.ua</a> ; <a href="http://www.quality.ua">http://www.quality.ua</a>
National Association of Milk Producers of Ukraine»Ukrmolprom»	Address: 1 B. Grinchenka str., Kyiv, 01001, Ukraine Tel./fax: +380 44 279 8389 <a href="mailto:email@ukrmolprom.kiev.ua">email@ukrmolprom.kiev.ua</a> ; <a href="http://www.ukrmolprom.kiev.ua">http://www.ukrmolprom.kiev.ua</a>
Union of Dairy Enterprises of Ukraine	Address: Office 410, 4a M. Raskovoi str., Kyiv, 02660, Ukraine Tel.: +380 44 451 4228 <a href="mailto:molsouz@i.kiev.ua">molsouz@i.kiev.ua</a>
Association Ukroliyprom	Address: 1 B. Grinchenka str., Kyiv, 01001, Ukraine Phone: +380 44 226 3138 279 6356 <a href="mailto:admin@ukroilprom.kiev.ua">admin@ukroilprom.kiev.ua</a> ; <a href="http://www.ukroilprom.kiev.ua">http://www.ukroilprom.kiev.ua</a>
Association of Ukrainian manufacturers "Ice cream and frozen foods"	Address: office 514, 5 Praz'ka str., Kyiv, 02090 Phone/fax: +380 44 2928293 <a href="mailto:aavm@aavm.com.ua">aavm@aavm.com.ua</a> , <a href="http://aavm.com.ua">http://aavm.com.ua</a>
Ukrainian Grain Association	Address: 4th floor, Predslavinska str., Kyiv, 01033, Ukraine Phone/fax: +380 44 2466764, 246 6799 <a href="mailto:inbox@uga.kiev.ua">inbox@uga.kiev.ua</a> , <a href="http://uga-port.org.ua">http://uga-port.org.ua</a>

Name	Contact
Informational-analytical agency "APK-Inform"	Address: 3rd floor, 21 Chicherina str., Dnipropetrovsk, 49006, Ukraine Phone/fax: +380 44 2783560 info@apk-inform.com, http://apk-inform.com
All-Ukrainian Association "Ukrainian Agrarian Confederation"	Address: office 807, 53/80 Saksagans'kogo str., Kyiv, 01033, Ukraine Phone/fax: +380 44 2876566, 289 9721
European Business Association	Tel.: +380 44 496 0601 Fax: +380 44 496 0602 office @ eba . com.ua; www.eba.com.ua
Agrarian Union of Ukraine	Address : office 504, 24 Khreschatyk, Kyiv, 01001, Ukraine Tel: +380 44 226-30-42, fax: +380 44 278-29-84; agrouu@gmail.com; http://www.auu.org.ua
Association of Farmers and Private Land Owners of Ukraine	Address: office 411, 21 Patris Lumumba str., Kyiv, 01042, Ukraine Phone: +380 44 5017873, 2284819 afzu@farmer.co.ua, farmasuk1@ukr.net, http://farmer.co.ua

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"Tachanka" PAC, phone: (05536)551-09

"Landtech" LLC, phone: (044)586-44-25

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