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THE GOVERNMENT INVESTMENT POLICY IN THE AGRICULTURAL SECTOR OF UKRAINE

Resume *In this article the main factors which influence the value of direct foreign investments and the role of the government in the field of the agrarian investments are investigated. In the result of our investigation we came to the conclusion that the government regulation of the agrarian investments in Ukraine should be based on the principles of active and passive regulation.*

Keywords: government investment policy, foreign direct investments (FDI), investment potential.

АНОТАЦІЯ *В статті досліджені фактори, що впливають на обсяги прямих іноземних інвестицій, обґрунтована роль державної політики у сфері інвестування в аграрному секторі економіки. Зроблені висновки згідно яким в основу державного регулювання інвестиційної діяльності у сільському господарстві України мають бути покладені принципи активно-пасивного регулювання.*

The relevance of research. During 2008 and 2009 the tendencies of global economy development have changed. The world financial situation at that period was characterized by the deepening of the debt crisis.

The deficit of investment resources became one its consequences which tended the finding of the alternative ways of financing. Thus the further economic development of the country now requires the direct investments based on the investment potential.

The recent developments. The problems of the government regulation and pursuing the investment policy in the agrarian sector of Ukraine were discussed by many scientists and economists, such as Kirilenko I.G., Komarov V.A., Lanченко E.O., Firsov E.A. and others.

The subject of research. Increasing the level of foreign direct investments is one of the ways of economic growth of agrarian enterprises. Nowadays there is a contradiction between the structural reconstruction of agrarian sector of economy with the help of investments and the low level of investments because of the high price for credit resources.

As a rule in the market economy the government plays a regulatory function. In realizing this function the investment policy formation should be among the major priorities of the government regulation in the world crisis context.

In the government investment research such methods as factor and investment analysis were used. The subject of studying is closely connected with the 'Mechanisms and instruments of Ukrainian internal and external economic policy regulation'.

The aim of research. The aim of the research is to prove that the agrarian enterprises need to be supported by the government and such support will increase the level of investments in the

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agrarian sector. The aim of the research is reached with the help of solving its tasks. One of them is the analysis of economic situation in the agrarian sector of Ukraine. Another one is the analysis of the main external funds according to their resources.

At present the government of Ukraine has to consolidate its actions directed to the lessening of negative influence of the world financial crisis on the economy of the country particularly in the agrarian complex. The final aim of these actions is to maintain the living standards of population of the country.

Thanks to the policy pursued by the government the consequences of the financial crisis were minimized and the main macroeconomic indicators were positive. In 2009 export of agricultural products exceeded import (Diagram 1) in which meat and meat products prevailed. In the export of agricultural products wheat predominated.

As it is commonly known, the currency devaluation is one of the financial crisis consequences. Among the others export-oriented branches of the Ukrainian economy an agrarian sector benefits most of all from hryvnya devaluation. For example, the prices for wheat have been extremely high in the domestic market this year; on the contrary these prices have been decreased in the world market.

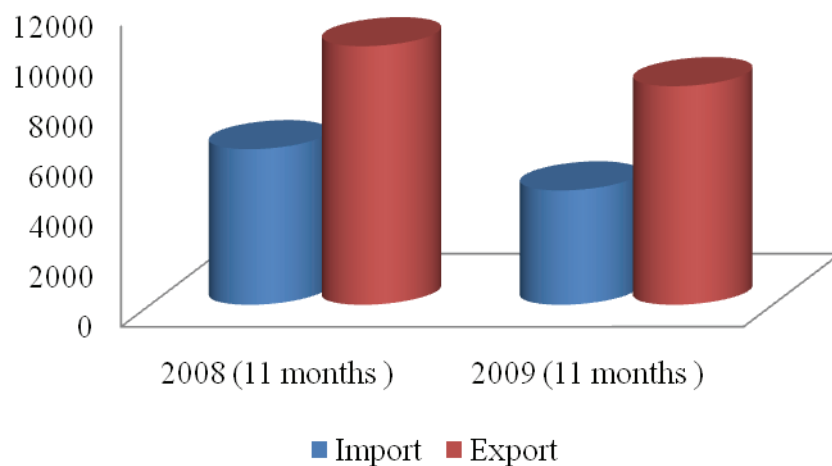


Diagram 1 Foreign trade balance of agricultural products in 2008-2009 (mln. hrv.)

As a result incomes of many agrarian enterprises increased and the costs cut down. And the rise of their profits will stimulate the further growth of the agrarian industry. As the agrarian sector takes a small part in GDP (for about 7-8% in 2008-2009) and the harvest is not stable from year to year its development does not greatly affect the Ukrainian economy.

It is also necessary to point out that the agrarian complex plays the significant role in the economy of Ukraine, as it is well known that the agrarian sector is one of the leading branches in the economy of the state. The geographical position of Ukraine, its soil and climatic conditions, resources and historical background define the industrial and agrarian tendencies of its further economic development [3]. Analyzing the ways of external financing of Ukraine it is possible to distinguish the most popular of them: bank loans, government support and investments.

1. Since it is commonly known the bank loans are the easiest and the most frequently used way of getting the external funds in the countries with the highly developed system of financial intermediaries. Financial intermediaries play a key role in improving economic efficiency because they help financial markets channel funds from lender-savers to people with productive investment opportunities.

Without a well-functioning set of financial intermediaries it is very hard for an economy to reach its full potential. As to Ukraine this source of financing is too expensive because of the high level of inflation. The main reason of low economic effectiveness of this kind of financing is the high payment on the bank credits and the absence of reasonable guarantees.

Table 1 Agricultural enterprises credits in 2008-2009

Indicators	2008		2009	
	mln. hrv.	%	mln. hrv.	%
Credits (total)	20053	100	5792	100
short-term credits	10300	51,4	4100	70,8
intermediate-term credits	6540	32,6	1150	19,9
long-term credits	3213	16	542	9,3

Loan funds are used by agricultural enterprises to cover outgoings and to purchase fixed agricultural assets including machinery for building and reconstruction of agricultural industrial facilities and acquirement of equipment for agricultural product processing. Agricultural enterprises obtained short-term loans - up to one year and intermediate-term loans - up to three years. In 2009 the credits given to the agricultural enterprises amounted to 5,8 bln. hrv., which made up 29 % compared to 2008: short-term credits – 4,1 bln. hrv., intermediate-term credits – 1, 15 bln. hrv., long-term credits – 55,7 mln. hrv. (Table 1)

Assistance in attracting of credit resources in agricultural sector plays an important role among the measures of state support. Nowadays soft loans account more than a half in total lending of this branch of economy (Diagram 2).

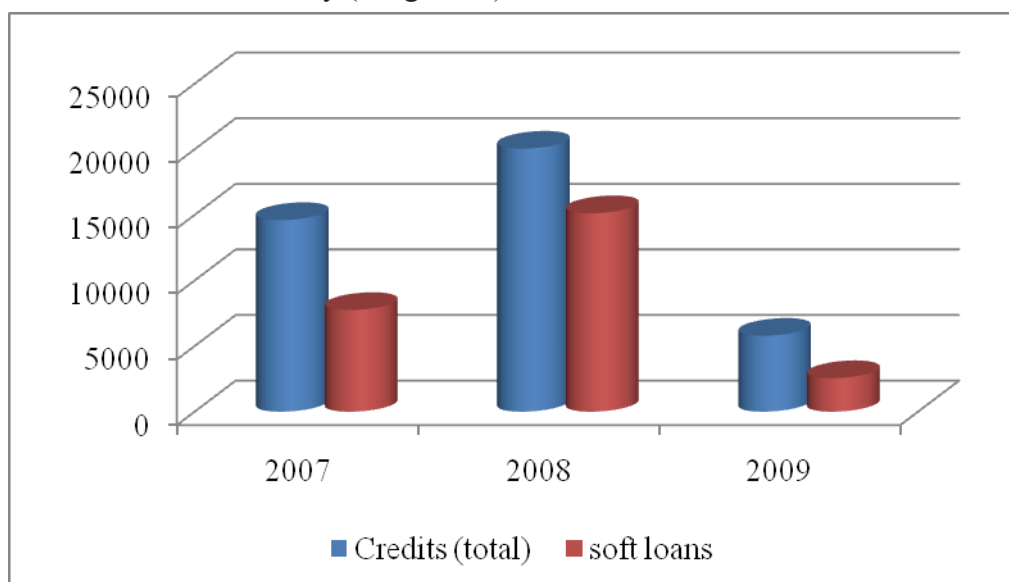


Diagram 2 Agricultural enterprises credits in 2007-2009 (mln. hrv.)

2. The government support is carried out with the help of investment policy which is considered as a complex of financial, legal and economic measures. The development or decline of the investment process is reached with the help of these measures. The forms of the government investment policy fall into two groups: active and passive regulation (Figure). The legal and economic measures belong to the passive investment policy when the government does not influence the investment process directly. The financial measures belong to the active investment policy when the government takes part in the investment process directly [4].

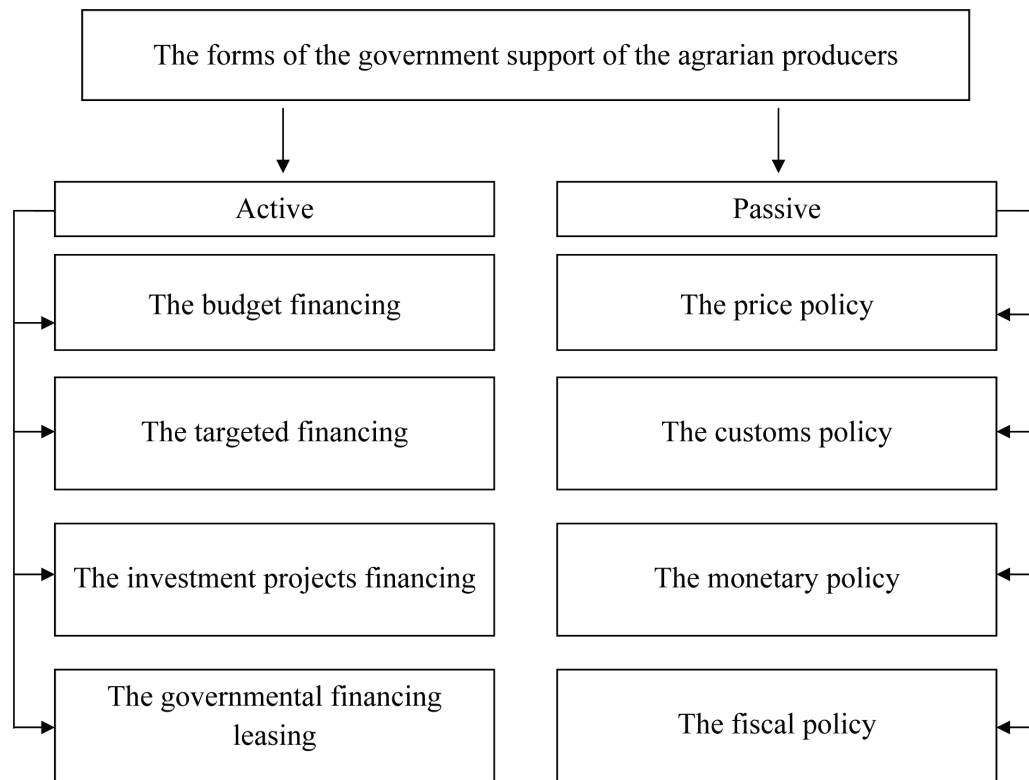


Figure. The forms of the government support of the agrarian producers

The important role in the organization of the investment process of the agrarian enterprises belongs to the state. The support of the government in the countries with market economy plays a regulatory function. The formation of the investment policy as a rule takes important place among the major priorities of the government regulation. With this in mind the government of Ukraine should intensify the investment support and regulation now in the terms of the world crisis.

Due to the government support to agrarian and industrial complex the total amount of state grants increased during 2006-2009 in Ukraine. In 2008 the volume of state grants exceeded 2 billion 921 mln. hrv., which is 500 mln. hrv. more compared to 2007 and 1 billion hrv. more compared to 2006. The volume of state grants accounted 441 mln. hrv. in 2009. For example, the European Union allocated for development of agriculture of France over 10 billion euro in 2008. Analyzing the structure of government budget costs in recent years it is possible to make a conclusion that the programs of financial support of stock-breeding and plant-growing predominated but there is a tendency of their reducing (Diagram 3).

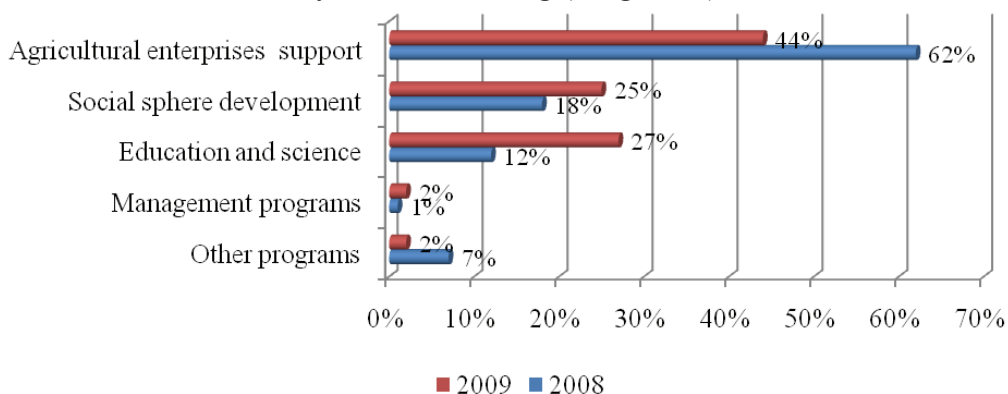


Diagram 3 Structure of budget costs of the Ministry of Agriculture of Ukraine in 2008-2009

Aimed at accelerated upgrading of machinery and tractor stock of agricultural commodity producers, the state finances the program to acquire the national agricultural machinery and equipment upon financial leasing terms and partially reimburses for the value of sophisticated agricultural machinery produced domestically. The national joint stock company "UKRA-GROLEASING" supplies the equipment/machinery on financial leasing terms and conditions.

Benefits of financial leasing include:

- 3,1% annual interest for the term of 3-7 years with 15% of the full value advance payment;
- annual interest rate is lower than on commercial credits;
- the pledge amount is considerably less compared to commercial banks;
- greater possibilities in using working capital;
- constant terms and conditions.

3. Investments including foreign investments are another way of getting the external funds. As a rule foreign investments are divided into two groups according to their forms: foreign direct investments and portfolio investing. As the financial market in Ukraine is not developed yet the foreign direct investments dominate in the structure of foreign investments.

According to foreign investors foreign investments are classified as:

- the governmental foreign investments;
- the investments of the international financial organizations;
- the private foreign investments.

The rise of the level of foreign direct investments is one of the traditional ways of economic growth of enterprises. It is important to notice that the private foreign investors in Ukraine are not active now, because of the low investment rating of the country. Thus the foreign direct investments are mainly provided by the international financial organizations, such as the European Bank of Reconstruction and Development and the Ukraine-Germany Fund.

The main investors of agrarian and industrial complex of Ukraine are: Cyprus (162,3 mln. dollars of the USA); Great Britain (74,2 mln. dollars of the USA); the USA (46,1 mln. dollars of the USA); Germany (34,6 mln. dollars of the USA); Denmark (32,6 mln. dollars of the USA); France (21,5 mln. dollars of the USA); the Russian Federation (20,5 mln. dollars of the USA).

The factors that influence the foreign direct investments are the following (Table 2):

Table 2 Structure of factors that influence foreign investments

	Internal factors	External factors
Inversely proportional quantities	1. Expected level of inflation 2. The interest rate on commercial bank loans 3. The presence of large organizational formations	1. The volume of import 2. The LIBOR rate
Directly proportional quantities	1. The volumes of internal consumption 2. The level of inner investments 3. The labour productivity	1. The government support of foreign investments 2. The development of the agrarian market and the level of competition

1. Expected level of inflation. It is considered that inflation rate and the direct foreign investing are inversely proportional quantities, as the higher level of inflation, the greater degree of the future income will devaluate. Therefore, the investors will have less stimuli to increase the volumes of their investments.

In August 2009 compared to July 2009 a consumer price index in Ukraine was 99,8%. In August 2009 compared to August 2008 consumer prices in Ukraine grew by 15,3%, as to the report of the State Statistics Committee. From the beginning of the year (August 2009 compared to December 2008) there was an increase in consumer prices in Ukraine by 8,2% . In January-August 2009 compared to January-August 2008 consumer prices in the country grew by 17,1% [8].

2. The interest rate on commercial bank loans. The wide range of interest rates in different countries is the reason of international flow of capitals, above all things in the form of portfolio investing. In 2009 annual interest rates in national currency diminished from 21,6% to 17,8% and in foreign currency it diminished from 12,6% to 10,1%. The credits given to the firms and companies grew by 3,9%, in 2009 as to the householders they reduced by 10,1% [5].

3. The presence of large organizational formations. For example, international investors support the creation of organizations in the form of the cooperatives in the countryside. The World Bank (WB) within the framework of the program on preparation of Poland to the entry to the EU halted financing of the projects related to the direct support of the separate agrarian firms. The WB gave the advantage of indirect support through the grants of investment credits for the development of agricultural regions as a whole and to introduction of the new technologies of production and realization of the programs of consolidation of the agrarian firms which were directed to the increase of the labour productivity.

4. The volumes of internal consumption. The majority of foreign investments are connected with industries which produce goods and services for an internal end consumption. The investors have to correct the volumes of investments taking into account the predictions of sale of goods which are planned to produce in Ukraine.

Thus, it is expedient to use the indexes of private consumption, because the foreign investors mainly orient to the industries which produce goods for private consumers (for example, food industry) [7]. Statistical data testify that the lowering of the level of private consumption in the second quarter of 2009 remained at the same level as in the first quarter of 2009, i.e. 11,6%.

5. The level of inner investments. It is considered that the volumes of the inner investing often serve for the foreign investors as an indicator of attractiveness of certain branches of economy and country as a whole. The increase of these investments testifies the growth of business activity and the willing of inner investors to expand the production. The main disadvantage of the investment climate for national investors is the low level of inner capital investments. It is generally known that the foreign investors will not inlay money in a country with such level of inner investing. In the second quarter of 2009 the decrease of investments in the fixed assets deepened by 57,8% [8].

In contrary the expulping of the foreign investments by inner investments is also possible as the participants of investment activity apply to the foreign investors because of the shortage of national savings. For example, as it was noted [2] bringing in and using foreign investments, including foreign direct investments are closely connected with the lack of financial resources.

6. The labour productivity. Even in the years of bloom of the collectivization of the agrarian sector of Ukraine, as a former republic of the Soviet Union, the labour productivity was seven times less than in agriculture of France, five times less than in Germany and ten times less than in Holland and the USA. Thus the contradiction between necessity of the investments for an update and retooling of material and technical base of production and investment opportunities is created. It is important to have the sufficient rate of return which is hardly to get because of the low efficiency of the use of available material and technical resources.

7. The volume of import. The export and investing are considered to be the alternative ways of cash flows abroad provided by the multinational companies. Therefore the volumes of foreign investments and import are defined as the inversely proportional quantities.

By the second quarter of 2009 the role of net export in the economy of the country became perfectly obvious. According to statistic data the adaptation of the current account transactions to the world prices has already taken place. For eight months of 2009 the current account deficit amounted 1,1 milliards of dollars, that is 7 milliards of dollars less than the sum of the current account in the same period of 2008 [8].

8. The LIBOR rate. It is well known that there is a reverse connection between the interest rate and the level of investments as an increase of interest rate reduces the rate of return of the investment project. Consequently, the LIBOR rate can be used as an indicator of the alternative cost for foreign investments. The LIBOR rate is closely connected with the deposit rate. The first one is possible to use for the correlation and regressive analysis.

9. The government support of foreign investments. The credit, price, fiscal, customs and insurance policies pursued by the government to stimulate the production of agrarian goods and the agrarian market development should be based on the new principles. To increase the investment rating of Ukraine and its investment potential two programs were worked out: "Programs of development of the investment activity for 2002-2010" and "The investment image of Ukraine".

10. The development of the agrarian market and the level of competition. According to statistic data the total volume of production of agricultural products in January-July 2009 compared to the same period of 2008 grew by 3,8%. In July 2009 compared to June the average prices for agricultural products decreased by 6%, the products of plant-growing dropped by 7%, the products of stock-breeding decreased by 3% [8].

Ukraine undertakes the measures to form agrarian market and develop its infrastructure. The infrastructure framework includes commodity exchanges, rural purchasing centers, urban wholesale and retail markets, cattle auctions, informational and marketing network, state monitoring system.

There are prior directions of investments in Ukraine supported by the government:

- Putting into operation of livestock buildings;
- Construction of storage facilities for fruits and vegetables;
- Construction of greenhouses for growing under cover;
- Construction of mixed feed, hay and silage structures;
- Land remediation.

Summarizing the main ideas mentioned above it is important to point out that the principles of active and passive government regulation are key elements of the government investment strategy in the agrarian sector of Ukraine. Therefore the government of Ukraine should support the development of the agrarian enterprises on this stage of economic growth.

The most of the Ukrainian scientists consider the formation of a favorable investment climate in Ukraine to be the main task of foreign direct investment strategy. According to the economists' point of view there are different ways of pursuing the investment policy. Among them are:

1. the financial governmental support of the agrarian and industry complex;
2. the price and monopoly state control;
3. the development of the agrarian market infrastructure;
4. the further development of the new forms of credit relationships, including forfaiting, factoring, discounting, and etc.

Conclusions. Finally it is possible to make a conclusion that the world economic crisis led to the negative tendencies in economy, especially in agriculture. As to the policymakers' opinion agriculture may become the leading branch of economy and stabilize the economic situation in the country in the context of the world economic crisis. There is no 'correct' strategy for economic development. Each country confronts a unique set of barriers and growth possibilities. The matter of great importance for Ukraine is to find its own way of economic development with the elements of both the market and former command economies taking into account the experience of the most competitive countries.

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