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Land Reform in Ukraine

The First Five Years

Csaba Csaki
Zvi Lerman

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Foreword

Agriculture in transition economies accounts for a much greater share of employment than in industrialized countries of Europe and North America. Agricultural reforms, which among other policies include privatization of land and restructuring of the traditional large farms, are therefore expected to be an important cornerstone for overall transformation of the economies of the former socialist world. The World Bank closely monitors the progress of land reform in these countries to evaluate the achievements, advise member governments on best practices, and design lending for investment and development.

Farm-level surveys provide one of the most effective monitoring tools that make it possible to penetrate beyond the anonymous curtain of official statistics. The World Bank, in cooperation with local research institutions, is conducting an extensive series of farm surveys in many of the former Soviet republics, including Russia, Ukraine, Moldova, Armenia, and Georgia. Farm surveys are also conducted across East Central Europe. The latest is a survey of Romanian family farms and farm associations. The results of these surveys are regularly published in the form of analytical reports in the World Bank Discussion Papers series.

The present study summarizes the first five years (1991-1996) of agrarian reforms in Ukraine. Although much has been accomplished in this period, it is our duty to note that much more remains to be done. Vigorous action with agricultural reform is required if Ukraine is to exploit its unique potential as an agricultural producer with one of the richest reserves of highly fertile soils in the world.

The findings and conclusions of this study should provide a useful tool for the Ukrainian government in assessing accomplishments and identifying future steps in agricultural reform. They also will be useful to international institutions designing financial and technical assistance, and to scholars studying the unprecedented process of transformation in transition economies. The World Bank will continue its commitment to provide the international community with similar analytical reports for other countries in transition.



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Preface

This report presents the results of a farm-level survey conducted in 11 provinces in Ukraine in January-March 1996. The survey constituted a continuation and an extension of a previous survey conducted by the Agrarian Institute in Kiev between November 1993 and March 1994, with support from the World Bank. As in the previous case, the survey included three questionnaires distributed to private farmers, managers of large farm enterprises, and employees of large farms. The sample was designed to cover the country from West to East, ensuring sufficient representation of the different agro-climatic and socio-cultural zones. The detailed structure of the sample is shown in **Table A**.

Table A: Structure of the Ukrainian Sample: 1996

Province	Zone	Private Farms		Farm Enterprises		Employees	
		Number	Percent	Number	Percent	Number	Percent
1 Kiev	Center	15	11.8	15	13.0	229	13.7
2 Cherkassy	Center	7	5.5	10	8.7	174	10.4
3 Sumy	North-East	15	11.8	15	13.0	227	13.6
4 Poltava	Center-East	10	7.9	10	8.7	150	9.0
5 Khar'kov	East	16	12.6	14	12.2	225	13.4
6 Donetsk	South-East	5	3.9	5	4.3	75	4.5
7 Kherson	South	14	11.0	14	12.2	218	13.0
8 Vinnitsa	Center-West	6	4.7	7	6.1	146	8.7
9 Ternopol'	West	14	11.0	15	13.0	225	13.4
10 Ivano-Frankovsk	West	10	7.9	10	8.7	5	0.3
11 L'vov	West	15	11.8	0	0.0	0	0.0
Total		127	100.0	115	100.0	1674	100.0

Source: Author's data.

The survey was part of a broader project on the topic of *Land Registration and Restructuring of Agriculture* funded by a PHRD grant made available by the Government of Japan through the World Bank. The survey was managed as a cooperative effort by a team of Ukrainian researchers in Kiev and a World Bank task team. The Ukrainian team conducted the field work, carried out data processing and analysis, and developed a comprehensive Russian-language report based on aggregate information and survey data. The World Bank team provided support in areas of survey design, computer software, data processing, and analytical methodology. The World Bank team also

produced the present English-language report, based on information provided by the Ukrainian counterparts and on independent analysis of the survey data.

The Ukrainian team was headed by P. Sabluk, V. Mesel'-Veselyak, and V. Yurchishin of the Agrarian Institute in Kiev. A. Fesina, also of the Agrarian Institute, acted as the administrative coordinator of the project. The various subject groups were headed (in alphabetical order) by N. Dem'yanenko (agricultural finance), N. Fedorov (land relations), N. Malik (intra-farm cooperation), V. Mesel'-Veselyak (farm organization), A. Onishchenko (land reform), N. Vdovichenko (social issues), and V. Yurchishin (agricultural policy). The project received wide support from the Cabinet of Ministers of Ukraine, the Vice-Premier's Office, the Ministry of Agriculture and Food, and the Ukrainian Academy of Agricultural Sciences.

The World Bank team included Csaba Csaki, Zvi Lerman, Mark Lundell, and Iain Shuker. Mark Lundell and Iain Shuker acted as task managers for the World Bank and provided administrative and financial coordination. Zvi Lerman directed the design and the methodology of the survey and was the principal author of the English-language report. Csaba Csaki provided scientific and policy guidance throughout the project and co-authored the present report. Valuable assistance with data processing and preliminary analysis was provided by Alexandra Sidorenko, during her tenure as a summer intern at the World Bank in 1996. Aleksander Kaliberda of the World Bank Resident Mission in Kiev assisted with coordinating the activities of the Ukrainian team. Golam Kirsch provided editorial comment and Alan Zuschlag prepared the report for publication.

The report starts with an introductory chapter, which presents a summary of the findings (Chapter 1). The legal framework for land reform and recent developments in Ukrainian agriculture are reviewed in Chapters 2 and 3, which are based on officially published sources. Chapters 4 through 8 are the empirical core of the study, presenting an analysis of the survey data. The analysis covers reorganization as seen by the managers of large farms (Chapter 4), the impact of reorganization on farm employees (Chapters 5 and 6), development of the new private sector in agriculture (Chapter 7), and financial situation of farm enterprises and private farms (Chapter 8).

Tables presented in the text without an explicitly identified source are based on the data of the present survey ("1996 survey," to distinguish it from the previous "1994 survey"). The data for all charts and diagrams are derived from the survey or from official aggregate statistics provided by the Agrarian Institute (the specific source is always clear from the context).

The present analysis of the 1996 survey complements two previous publications that analyze the findings of the 1994 survey. The English-language publication is *Land Reform and Farm Restructuring in Ukraine*, World Bank Discussion Paper 270, The World Bank, Washington, DC (1994). The parallel publication in Russian is *Zemel'naya Reforma i Reorganizatsiya Sel'skogo Khozyaistva v Ukraine*, World Bank Discussion Paper 270R, The World Bank, Washington, DC (1995). Both publications are available from the World Bank Bookstore, 1818 H Street NW, Washington, DC.

Abstract

By 1996, the state had transferred most of the agricultural land in Ukraine to collective and private ownership, but 40% still remains in state ownership. The individual sector, including household plots and private farms, has increased its role significantly, and it now cultivates 15% of land in the country and accounts for a substantial share of products sold in the marketplace. Yet the growth of private farming has slowed down after a vigorous start, and the number of independent family farms appears to have stabilized at around 33,000, at least temporarily.

Internal restructuring of collectives is only beginning. The distribution of land and asset shares has been completed in about half the farms surveyed, and most farms still retain central management without radical reorganization into internally autonomous subdivisions. The new shareholders and other employees fail to discern significant changes following formal reorganization of their farm enterprises. Ukrainian agriculture remains dominated by large collective structures that continue to operate according to old principles, and the recorded diversity of new organizational forms is nothing more than a result of “changing the sign on the door.”

The failure of large farms to adapt to new economic conditions has resulted in a distinct deterioration of their financial performance. The new private farms, on the other hand, appear to be fairly profitable. Families of independent farmers in general are much more affluent and more optimistic than households of employees in farm enterprises. Yet most rural residents prefer to invest their land and asset shares in the local farm enterprises rather than risk private farming.

The findings of the study suggest that land reform in Ukraine is in a danger of stagnation. The government must make every possible effort to create the necessary institutional and market conditions for injecting the stagnating reforms with renewed vigor.

Executive Summary

March 1996 marked the five-year anniversary of land reform in Ukraine and the beginning of the attempts to transform the agriculture and food sector into a more efficient and productive system based on market principles and private ownership. In addition to land reform and restructuring of traditional collective and state farms, the agenda of sector reforms includes liberalization of the market environment, privatization of agroprocessing and trade, and the creation of a new institutional framework for agriculture.

Measurable progress has been achieved in all areas of reform. However, the progress has not been smooth. The pace of agricultural reforms has been characterized by a continuous struggle between pro-reform and conservative forces since Ukraine became an independent country. Because of the resulting tensions, the government has been unable to implement a consistent set of policies required to address properly the most critical reform issues.

Land reform, which is one of the major components of the reform process in Ukraine, is the primary focus of this report. The study is based on the results of a farm-level survey conducted in 11 provinces in Ukraine between January and March 1996. The survey constituted a continuation and extension of a previous survey conducted by the Agrarian Institute in Kiev between November 1993 and March 1994, with support from the World Bank. The objective of the study has been to conduct a rigorous empirical and analytical assessment of changes in land ownership and farming structures, and to evaluate the impact of restructuring in large-scale farms since independence through spring of 1996.

Declining Sectoral Performance

The overall performance of the sector indicates that reforms have not yet succeeded in improving efficiency and productivity. In fact, *sectoral output, investments, and the level of technology continue to deteriorate*. The initial expectations that market-oriented economic reforms will produce a fast supply response leading to rapid recovery have not materialized in any of the former socialist countries. In Ukraine, as in many other transition economies, the years since 1990 have been characterized by an overall decline in economic activity, and in particular by a decline in agricultural production. The gross domestic product in Ukraine dropped by 1996 to 43% of the 1990 level. Agricultural production declined somewhat less precipitously, dropping to 59% of the 1990 level. Despite the slower decrease in the volume of agricultural production, the share of agriculture in the economy calculated at current prices shrank from about 24% in 1990-1991 to 12% in 1996. While production and market share declined, the agricultural labor force remained unchanged at five million, or about 20% of the total number of employed. So far, declining output has not been accompanied by adjustment in labor resources, probably because of a lack of alternative employment opportunities in rural areas, and in the country as a whole. This certainly has had an adverse effect on the efficiency of agriculture.

The crop sector, where Ukraine has its major comparative advantage, has suffered from an overall decline. Sown areas have not changed dramatically since 1990, and yet the production of the main cash crops, cereals and sugar beets, dropped by 30%-40% between 1990 and 1995. Grain output declined from 50 million tons per year to less than 30 million in recent years. This has been the result of a marked reduction in yields, probably due to general deterioration of farm input supply systems and mechanical services during transition. The efficiency of production as reflected in all standard measures (i.e., the ratio of labor to output, crop yields, milk yields, and weight gain of animals) has clearly deteriorated.

Signs of decline are particularly visible in the livestock sector. Livestock production traditionally accounted for 55% of gross agricultural product; it has now shrunk to 45% of total output. The decline in production has been much greater than the decline in the number of animals, pointing to deterioration in the efficiency of the livestock sector.

Slow Progress in Land Reform

The process of land reform and farm restructuring in Ukraine is far from progressing vigorously. The only major accomplishment is the transfer of state land to collective ownership, and even this undertaking remains uncompleted. Distribution of land shares to individuals in collective farm enterprises is less than half complete, and internal restructuring of the formally reorganized farm enterprises has hardly begun. ***Farm employees report that the overall situation in their enterprise has remained largely unchanged after reorganization.*** In the few cases where farms have reorganized into smaller structural subunits, the autonomy of the new subunits is extremely limited and the enterprise in effect continues to be run by central management.

Two encouraging signs are the increasingly commercial orientation of household plots in collectives and the generally profitable situation of independent private farms established outside the collectivist framework. Yet despite the generally favorable well-being of private farmers, farm employees do not show much enthusiasm to exit collectives and start private farming. ***Farm employees prefer to stay in collectives,*** at least for the time being, although they are highly dissatisfied with the well-being and income of their families. In this respect, Ukrainian peasants are no different from peasants the world over, who are notoriously conservative and do not like exposing themselves to new risks.

After five years of reforms, only 15% of agricultural land in Ukraine is cultivated by the individual sector (household plots and family farms), and ***most Ukrainian agriculture remains effectively collectivized, despite the diversity of organizational forms that have emerged since 1992.*** Moreover, the growth of private farming has slowed down considerably since 1994, and the number of private family farms appears to have stabilized, at least temporarily, at 33,000, with 2% of agricultural land and about the same share of agricultural product. The overall impression from the findings of the survey is that ***land reform in Ukraine is in danger of entering a stagnation phase.***

The government needs to make every possible effort to create the necessary conditions for injecting the reforms with renewed vigor.

Changes at the Farm Level

The survey was designed to go beyond official statistics and capture information on the progress of land reform at the farm level. Interviews with managers of large farms and with individuals in rural communities provided first-hand evidence on major characteristics of the reform process, as viewed by different participants. The survey of some 2,000 respondents addressed the following main issues.

- **Does reorganization in large farm enterprises go beyond simply “changing the sign on the door?”** Although most land has been transferred from state to collective ownership and farms are now registered in a wide array of different organizational forms, internal restructuring has been minimal. The sector continues to be dominated by collective farming structures that are largely managed by traditional centralist means, and individuals fail to discern significant internal changes as a result of reorganization.
- **How far have individuals in rural communities advanced toward assuming responsibility for their property rights in land and assets?** Distribution of land and asset shares to individuals is progressing, although it is still only half complete. The shares, however, are still mere paper certificates, and no mechanisms have been developed to institutionalize selling or leasing of individually held shares in land and assets to entrepreneurial farmers or active producers. Rural residents by default leave their shares for the use of the former collective. Although every individual is guaranteed the right of exit from the collective enterprise, private farmers generally report that they have left their former collective without any entitlement of land and assets.
- **To what extent does the individual sector engage in commercial rather than subsistence farming?** Private farmers show a definite commercial orientation, which is reflected in a pronounced adjustment of their product mix, emphasizing crop production at the expense of livestock. Household plots also sell a substantial proportion of their output in local markets, and derive around 20% of family income from sales of farm products. There are no signs that Ukrainian agriculture is reverting to subsistence farming.
- **How accessible are various market services to agricultural producers?** Private suppliers and marketers are emerging, and small-scale producers are beginning to use private traders as a source for their inputs and an outlet for their products. These encouraging developments notwithstanding, the traditional state monopolies (now transformed into privatized monopolies) continue to dominate agricultural processing, marketing, and input supply.
- **What has been the impact of reform on the individual in rural areas?** Independent private farmers are much more satisfied and optimistic than rural residents who stay on as

members and employees of collectives. Yet, despite the dissatisfaction of the membership of collective farms with their well-being and family income, most of them prefer to remain under the safety umbrella of a collective organization and are not prepared to accept the new risks of independent farming.

What Are the Prospects?

The accomplishments of Ukraine in reforming agriculture, and specifically in land reform, have so far been modest. The present analysis confirms the underlying reasons for the slow pace of change first identified in the previous report on land reform in Ukraine in 1994.¹

Initial accomplishments in the process of reform have been modest for a variety of reasons:

- **Political and legal uncertainty:** Controversy over the outline of the general reform program has distracted the attention from the sectoral agenda, and frequent changes of legislation have created a sense of uncertainty about the future course of reform.
- **Lack of a supportive environment:** Functioning markets for farm inputs and products have not yet emerged, which impedes successful operation of the new privatized agriculture. The financial sector is in disarray, few banks are able to provide mortgages, and few landowners are willing or able to offer land as collateral. Mortgage finance is an important instrument of agricultural lending for private investment, but its development requires security of tenure, legal title to land that can be used as collateral, and existence of land markets that provide an objective valuation of land. Land markets do not function at present because sales of privately owned land are still subject to a moratorium, despite repeated attempts by the government to change the law. Fully functioning land markets, including unconstrained purchase, leasing, and mortgage of land is necessary if Ukraine is to develop its potential for high-yielding, high-value agriculture, which is consistent with its natural endowment and is essential for supporting rural incomes.
- **Inadequate mechanisms for restructuring and exit:** Procedures for further restructuring at the farm level are still inadequately developed, and individuals and farm managers lack basic information about the available options. According to respondents in the study, the mechanism for exiting collectives with land and assets is not yet operational. Procedures have to be developed for groups of shareholders to present a proposal of separation, or less radically a proposal of internal regrouping, including specification of the land and assets the group would like to receive for its use. Procedures are also needed for adjudication of

¹ Z. Lerman, K. Brooks, and C. Csaki: *Land Reform and Farm Restructuring in Ukraine*, World Bank Discussion Paper No. 270, Washington, DC (1994).

disputes that arise when the remaining shareholders do not approve a specific separation proposal.

- **High risk and lack of instruments for risk management:** Political uncertainty, lack of clarity in program design, and macro-economic instability create a risky environment for private farming, and yet even such basic instruments as secure savings and insurance are not available. Continued high inflation increases the risk for agricultural producers, and encourages the retreat from markets into internal distribution and inventory accumulation. Participants in land reform and farm restructuring are likely to opt for remaining within larger collective units, where distributions in kind provide a hedge against erosion of cash incomes.

Unfortunately, the current procedures for land reform and farm restructuring do not yet provide a flexible framework for effective implementation. Nor is the environment created by the macro-economic reforms and the overall privatization program supportive of vigorous agricultural reform. Developments in Ukraine confirm that reforming socialist agriculture requires a consistent set of coordinated actions. Overall progress can be expected only if coordinated reforms are implemented completely. Land reform is obviously a major, yet not the only, determinant of a successful transition. Progress in land reform and the completion of the transformation of agriculture to market-based operation requires the government of Ukraine to address effectively the following main issues:

- **Continuation of restructuring of former collective and state farms to create market-conforming, efficiency-motivated units.** Farm restructuring has to enter a new phase, ensuring genuine reorganization based on market-oriented operation and incentive systems that encourage individual accountability. Strict financial disciplines must be enforced to initiate changes in all farming organizations that are unable to operate efficiently. In addition to efforts promoting independent family farming, the creation of other genuinely private producer structures and service cooperatives must receive more attention.
- **Introduction of changes in the legal framework governing land ownership and transactions in land.** The moratorium on the sale of land should be abolished without further delay. The prevailing restrictions on private ownership of land are a serious obstacle to the creation of market-oriented farming through regrouping of land and assets. Prohibitions on transactions in land also inhibit financing and investment in agriculture. Leasing arrangements should be contractually formalized, and lessees (whether individuals or collectives) should pay for the use of leased land. At present, many lessees use land and pay for it indirectly or not at all. Much of the leased land originates from the state reserve, and in practice the lease is simply a permission to use the land, rather than a commercial agreement. Development of lease contracts is particularly important for the emergence of efficient farming units as long as markets for buying and selling of land remain rudimentary.

- **Improvements in the market environment.** Although the creation of functioning market institutions takes time, the regulatory and market environment can be improved quickly by removing the remaining export barriers and the remnants of the state-order system, especially the continued intervention of the regional authorities in farm-level decisions. To promote agricultural markets for both private and state-owned enterprises, all state agricultural procurement needs to be carried out on a competitive basis, through open tenders and purchases on commodity exchanges. Intermediaries and marketing enterprises need to be encouraged to participate more widely in the agricultural commodity exchanges to increase competition for output from agricultural enterprises, which do not usually have the trading expertise for direct access to commodity exchanges.
- **Demonopolization and privatization of the grain sector.** The grain distribution system, and grain trading in general, represent the most critical component of agricultural markets in Ukraine. Grain, and especially wheat, is viewed as a strategic commodity for reasons of food security, as well as for its role as one of the commodities that pays for imports of natural gas. Demonopolization requires vigorous policy monitoring and advocacy to ensure a “level playing field” for state and private enterprises.
- **Rehabilitation of agroprocessing and input supply.** Privatization in these subsectors should be accelerated to create transparent ownership and management within a truly competitive framework. Without an internationally competitive agroprocessing sector, primary agriculture cannot develop its full potential. Transition from former state monopolies to new private monopolies, as it is often practiced today, is not a solution. Foreign investments essential for facilitating the technological renewal of agroprocessing can be obtained only if investors are able to function in a business-oriented competitive environment. Privatization of agroprocessing, marketing, and input supply falls outside the purview of land reform. Yet the current situation indicates that a modern competitive agroprocessing industry is an essential precondition for the success of land reform.
- **Reform in financial services and availability of capital.** Financial sector reforms should be accelerated, in parallel with the rehabilitation of agroprocessing and trade. Functioning financial institutions are essential for providing short-term and long-term funds to agriculture. Strict financial discipline should be imposed on all farms, as well as other enterprises, so that accumulating arrears do not undermine the reforms and distort incentives to which managers respond.
- **Creation of a new supportive institutional framework.** The strengthening of public institutions and improvement in the provision of public goods and services for privatized agriculture is also an essential condition for the ultimate success of land reform.

If these issues are addressed effectively, Ukrainian agriculture will be able to advance to the second stage of the overall land reform and farm restructuring program, which involves *creation of market-oriented, profit-motivated structures based on clear individual ownership of land and assets and*

an incentive system that encourages individual responsibility and rewards individual effort. The new farm structures may take a variety of forms. Some person will exit individually with shares of land and assets and establish private farms. Others will pool their shares and create small partnerships or cooperatives for farming. Yet others may choose to lease their land to more enterprising producers and assume the role of “inactive investors”, or alternatively focus on development of private farm-support services. The former collectives will gradually break up into individual farms or small farming groups, where production will be based on privately owned land and assets. These new producers will be supported by market services, some of which will be provided by new private entrepreneurs (individually or in groups), while others may be based on former collective management structures that will redefine their role as service firms or cooperatives.

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