

**THE FORMATION OF EFFECTIVE RESOURCE SUPPORT OF  
AGRICULTURAL PRODUCERS THROUGH THE DEVELOPMENT OF  
FINANCIAL AND CREDIT RELATIONS IN UKRAINE**

**Annotation**

*In the article the basic problems of financial and credit relations in the agricultural sector of Ukraine at the present stage of development are revealed and the ways to achieve effective resource support of agricultural producers through the development of financial institutions are discussed.*

**Key words:** agriculture and agricultural enterprises, lending, financial mechanism, commercial banks, credit risks.

**Анотація**

*У статті розглянуто основні проблеми фінансово-кредитних відносин у сільськогосподарському комплексі України на сучасному етапі розвитку, визначено шляхи досягнення ефективного ресурсного забезпечення сільськогосподарських товаровиробників за допомогою розвитку системи фінансово-кредитних установ.*

**Ключові слова:** сільськогосподарський комплекс, сільськогосподарські підприємства, кредитування, фінансовий механізм, комерційні банки, кредитні ризики.

**Аннотация**

*В статье рассмотрены основные проблемы финансово-кредитных отношений в сельскохозяйственном комплексе Украины на современном этапе развития, определены пути достижения эффективного ресурсного обеспечения сельскохозяйственных товаропроизводителей с помощью развития системы финансово-кредитных учреждений.*

**Ключевые слова:** сельскохозяйственный комплекс, сельскохозяйственные предприятия, кредитования, финансовый механизм, коммерческие банки, кредитные риски.

**Introduction**

Changes in the financial mechanism, caused by the dynamic development of the environment and the need for the farm entities to be adapted to the market conditions, require new approaches to their credit relations. Currently, there is the controversial approach towards the definition of factors that hinder the development of these relations and the priorities of farm entities' crediting process. One reason for it is not an explicit theoretical and methodological study of these processes along with the practices of bank lending to agro formations.

For a long time agricultural complex of Ukraine had been operating in the conditions of low logistical security. Poorly developed credit market and therefore the lack of funding money is the remarkable obstacle for its rapid development. One of the most critical problems is the lack of role of commercial banks in lending to agricultural producers. As the result the potential for the development of agriculture complex cannot be used to its fullest.

Under modern conditions, when on the world market there is a growing demand for food, an extremely important task is the further development of domestic agriculture on the direction of strengthening the material-technical base, also through the establishment of credit processes for agricultural enterprises.

Thus, the formation of the effective mechanism for crediting agricultural enterprises, which would be able to meet the high demand in the market of crediting agriculture and to overcome the tendency of low offers on loans by commercial banks, is the priority goal for the development of agricultural sector.

**Statement of research objectives**

The purpose of the article is to analyze the main problems of financial and credit relations in the agricultural sector of Ukraine at the present stage of its development, to identify ways to achieve the effective resource supply of agricultural producers through the development of financial and credit institutions.

## Results

One of the fastest growing sectors of the Ukrainian economy is the banking one, which demonstrates high numerical growth in the scale of its activities and significant impact on all parts of the economic system. An important role in the development of economy in general and the agricultural sector in particular in Ukraine plays the relations between agricultural enterprises and banking institutions. The development of agriculture is impossible without bank lending, which is ensured by the tendencies of the economic cycle and financial resources associated with the peculiarities of their circulation [4].

It is clear that agricultural lending is inherent with high risks, which increase even more through the following specific features: agricultural production is seasonal, with the long production cycle, the time of investment in resources, production and reception of products in most agricultural areas is separated by at least 6 months, agricultural production, despite of technological progress, is in a strong dependence on climatic factors (drought, floods, epizootic, etc.), the existing disparity in prices is not in favor of agriculture and so on.

The objective necessity for crediting agricultural enterprises is due to the existence of seasonal needs for additional working capital in ensuring the continuation of its movement. With the help of the short-term loan, agricultural enterprises as the rule cover the difference between the overall need for financial resources and their existing volumes. Thus, the credit provides stable conditions for economic activity while acting as the balance feature of financial resources.

Despite to some progress in the development of crediting process into the agricultural sector in recent years, lending is still far from the needs of the sector and the credit mechanisms are not perfect, neither in terms of protecting the interests of borrowers nor the security of financial institutions providing loans [3].

In addition, during the process of providing bank loans there is the lack of knowledge and experience of the borrowers in order to properly present the status and capabilities of their business and to assess the validity of the requirements which are put towards them by lending institutions. On the other hand, due to the inadequate legislation and slowness of the judicial system, credit institutions have very limited access to debt recovery, and, consequently, they compensate high risks of loans by imposing strict requirements for borrow-

ers and higher interest rates.

It should also be noted that by this time most of the credit market problems remain unsolved. First of all we are talking about improving the legal framework that governs the legal, financial and credit relations in the agricultural sector and the further development of credit institutions. Thus, the questions of land ownership, undeveloped market of land use, significant deterioration and moral obsolescence of fixed assets remain unresolved. It is known that the absence of the market of land prevents its use as the collateral for the loan, which in turn impedes the development of the long-term lending.

One must also intensify the new forms of crediting in the agriculture which will enable getting commercial loans without the direct government involvement. An example of this would be obtaining loans which are secured by manufactured products, factoring transactions, loans by promissory notes and financial leasing.

Now the functions of the credit-deposit servicing of the agriculture in Ukraine are being performed by unspecialized commercial banks, which are seeking minimal risk of their capital investment into the agricultural sector [5].

At the same time, examples of successful activities of foreign banks in many countries in the agricultural sector indicate that they have learned to effectively manage their risks. Among the factors that contribute to this are the following:

- the analysis of projects and the solvency of rural households;
- gradual structuring: from small loans to re-lending larger reliable borrowers;
- the diversification of loan portfolio;
- the combination of group and individual lending technologies;
- the expansion of activity in remote areas by working with credit unions
- providing financial services of attracting deposits and loans;
- the creation of effective incentives for staff and borrowers in order to ensure the timely repayment of loans.

Agricultural producers may prefer the traditional cultures and technologies which are less profitable, but more reliable and stable in order to manage risks and minimize them. However, under the condition of proper encouragement they can also complement the current crop of potentially risky cash crops, which will give more profit. In addition, budgets of farmers and small businesses

are largely integrated with the finances of their households, so the total cost of agricultural production, consumption, social goals can be directly linked. In many cases, the bias of the bank employees in regards to insurmountable problems of agricultural crediting has become a disaster, because due to this situation this type of credit is either categorically excluded, or very complicated to receive and more expensive [1].

There is a compromise between diversification and specialization. The access to the world markets induces producers to implement highly specialized, growing high-yielding varieties and getting revenue and profit from economies of the scale production. Maybe they will have to use the mechanisms of risk management (such as insurance, price stabilization means, and futures) in practice for diversification in favor of small scale activities and transition to a narrow specialization. Non-financial institutions and government can take an active part in such risk management in order to stimulate investment in the commodity of sub-sectors and encouraging the inflow of funds from the private sector.

Experience of the developing countries also confirms that most financial institutions, including commercial banks, are avoiding cooperation with enterprises of agriculture. Mostly it is a consequence of the financial policy of restricting risk or poor management. On the other hand, this experience also suggests that the reformed and well-managed specialized agricultural financial institutions can provide a favorable and stable credit of commodity production, processing and trade. These institutions include banks, agricultural development (China, India, Iran, Indonesia, Pakistan, Algeria, Tunisia, etc.), rural banks (in Nigeria, Ghana, Tanzania, Philippines, Indonesia), financial cooperatives (in Kenya, Tanzania), rural funds (in Syria, India, Indonesia) [2].

For these institutions and their customers financing the agricultural sector is an attractive business. Their experience also showed that social and economic objectives of rural and agricultural development are best achieved not through charity, but with the help of financial relations between the institutions and their customers based on commercial principles.

Such entities may advantageously provide commodity loans: not as a single service, but as part of sustainable profitable loan portfolio. Therefore the limits of credit process are being gradually expanded, balancing between a purely

commercial projects and projects of social and economic development.

Although agricultural credit inherent in the particular problems of modern agricultural development, banks can effectively overcome them. These institutions have developed risk management strategies for agricultural credit and other rural projects [7].

The essence of the strategy of credit risk management for agricultural borrowers lies in their systematic detection and minimization.

Some lessons for the development of domestic financial mechanism of the agricultural sector can be taken from the experience of successful foreign banks in agricultural development. These, above all others, are:

- the thought-out and effective financial policy that works and promotes innovation;
- the attractive banking products savings and loan with appropriate stimulation of employees, effective system of internal control and supervision ensuring high profitability of rural micro-credit;
- the poor segment of the population can save, and rural financial institutions can mobilize these resources with minimal cost;
- if financial services are being provided without stimulation of lending, the demand for deposit savings exceeds the demand for loans with a large «plus»;
- the incentives for the timely repayment of credits, which work effectively;
- the coverage from the side of the financial institution of a huge number of people with low income combined with competitiveness, breakeven point, and financial independence of the bank;
- high transaction costs can be reduced by increasing the amount of loanable funds [6].

Agricultural development banks in many countries are viable and sustainable providers of financial services to all segments of the rural population, including the especially poor ones, fulfilling an important social and economic mission.

### Conclusions

A lot of factors that effect the development of the process of bank lending into the agricultural sector can be divided into two groups: factors that are determined by the specific features of agricultural borrowers, and the factors governing the economic and legal relations of banks and borrowers. Of course, not all factors are equally having positive effect on the willingness of commercial banks to lend money to agricultural enterprises.

Some factors, due to the specifics of the agricultural businesses in our country, limit the number of credit portfolio, as well as increase the riskiness of both the agribusiness and the related bank loans.

One of the features of crediting agricultural borrowers is the significant complexity analysis and control of business borrowers, connected with their diversified activities (each company has several types of activities: crop, livestock, horticulture, vegetable growing, etc.).

Moreover, taking into account the lack of specialists with agro technical education in banking institutions, banks are forced to engage seasonal monitoring of future harvest (mortgage) agronomists and animal husbandry, which increases the cost of bank credit operations.

The use of future crops and livestock offspring as the collateral for the provision of the credit increases the credit risk, as the early realization of collateral is almost impossible. Moreover, the specificity provided requires more active formation and development of the market of forward and futures contracts as well as the insurance market in Ukraine.

During registration of the future harvest the seizure of the collateral can usually be done only after the harvest has been collected. Thus, in case of adverse weather conditions the non-assembled yield may die, and the borrower will lose not only

a source for repayment, but also the collateral that serves as the security for fulfilling obligations before the bank. Therefore, taking into account the high dependence of agribusiness on natural factors, one of the ways to minimize the credit risk is insuring the crop.

Ukraine should have the strong agricultural sector in order to address the difficult socio-economic tasks and goals and ensure the food security. The system of financial institutions should contribute to the effective resource support of agricultural producers and the formation of new government policy regarding financial relations in the countryside, progressive forms of financial support of the agrarian sector of economy in consideration with international experience in this sphere.

In order to achieve this goal it is essential to:

- strengthen political will for legislative regulation and the creation of appropriate regulatory framework;

- create and implement an adequate strategy for reforming agricultural production;

- create and implement an effective system of financial services provided to farmers, with branches representing profit centers;

- to provide operational and financial stability;

- to ensure the effective internal control and external bank supervision

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