

## Construction of Effective Livestock Insurance Model in Ukraine

### Research Article

O. Alshanova<sup>1\*</sup>

<sup>1</sup> Department of Animal Husbandry of Ministry of Agrarian Policy and Food of Ukraine 24, 01001, Kyev, Ukraine

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\*Correspondence E-mail: [816@minap.kiev.ua](mailto:816@minap.kiev.ua)

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### ABSTRACT

The problem of food security during the last few decades has acquired a global character. Population growth, reduction of farmland suitable for agriculture and ecological factors has led to a sharp increase in food demand. In such conditions, the role of countries which are able to increase the export of agricultural production in short-term periods is rising. Ukraine has great opportunities for the agricultural production because of favorable climatic conditions and strong human resources. However, the existing potential of the agricultural sector is mainly in the crop, which significantly reduces the competitive strategies of Ukraine in the world market. The absence of effective mechanisms of insurance protection is one of the important factors which hinder the development of livestock in Ukraine. The world experience shows that livestock insurance turned into current state policy supports the agricultural sector. Ukraine's integration into global agricultural market provides the applying of unified livestock insurance mechanisms which proved their capacity in other countries. At the present stage, the state prefers other forms of entrepreneurship support in livestock-through price regulation, subsidization and the facilitation of access to financial resources. At the same time, Ukrainian companies operating in the agricultural sector need insurance protection. Implementation of livestock insurance's foreign experience in Ukraine is complicated by the absence of effective agricultural marketplaces and appropriate market infrastructure. The current state of public finances significantly reduces the probability of successful implementation of the system scenarios livestock insurance based on the active use of central funds. Therefore, Ukraine should make an effort to meet demand for insurance products from the side of livestock producers with the minimal use of budget funds. That is why it is necessary for the state to create conditions for the formation and operation of effective model of livestock insurance and providing optimal solving of current tasks of this sector's development.

**KEY WORDS** agricultural market, livestock insurance, Ukraine.

### INTRODUCTION

With the globalization of the world economy, the food problem - with overproduction in some areas and significant deficits in others - demands new approaches are needed in livestock insurance. Their peculiarity, first of all, is in the use of common rules and mechanisms within the cross-border cooperation, economic blocs and alliances. The catastrophic scale of individual risks in livestock causes trends to enhance cooperation in the sphere of livestock

insurance. The analysis of a number of studies shows that animals' diseases are transformed in one of the main problems of agricultural sector from the beginning of XXI century, which has significant economic and social consequences for the society (ISPRA, 2006). Herewith, such problems are typical as for the countries with high level of economic development (Eckhard Engert, 2006) and for developing countries (Mahul and Skees, 2006). In Ukraine currently livestock insurance use is rare and unsystematic. Insurance companies do not offer attractive insurance prod-

ucts on the market, and in turn, farmers do not demand insurance, but use other methods of risk management. The problem of choice of Ukraine's strategic priorities is ongoing. On the one hand, Ukraine has the prospect of signing an association agreement with the European Union, but on the other hand, Ukraine may join the Customs Union. The choice of the given alternatives will determine the further development of agricultural insurance in Ukraine, because in the frameworks of these economic blocs, different approaches are used to cooperate in the field of animal health and their insurance.

## MATERIALS AND METHODS

The dialectical method was used in the process of research for the determination of the current condition of livestock insurance in Ukraine. The methods of analysis and synthesis were also used for assessment of prospective of insurance in livestock in Ukraine.

## RESULTS AND DISCUSSION

Results of Ukraine's economy reforming in general do not justify those expectations that arose during the period of obtaining independence in 1991. The State, for a variety of reasons, failed to solve important economic and social problems connected primarily with unstable economic development and overcoming of economic inequality among different population groups. During a long period state policy was aimed at supporting traditional economics sectors – metallurgy and chemicals. Such a strategy allowed restoration of economic growth in Ukraine at the beginning of XXI century.

However, it is connected with great risks, including the formation of interdependence between macroeconomical dynamics in Ukraine and trends of particular global markets' development. Moreover, this strategy does not give the opportunity to overcome evident technological backwardness of Ukrainian industry [Dufhues et al. \(2004\)](#).

For a long time, the agriculture sector was seen not in the context of strategic state policy on the global economic arena, but only from the standpoint of satisfying domestic demand for food. However, dynamic changes in the world agricultural market forced a reassessment of these approaches. In recent decades, food security has become one of the key problems at the world level. Uncontrolled growth population and environmental problems that reduce the availability of arable lands are the main factors for increasing demand for food and for significant increases in the prices of food. Ukraine is justifiably considered one of the most valuable players of world food market. With significant natural potential and experience of management in the

agricultural sector, the country is able not only to quickly fill the domestic market, but also to accumulate great food volumes for global purchase and consumption. Reduction of the agricultural sector's role in the formation of GDP during the period of 2004-2007 is the consequence of active development of metallurgy production. However, since 2008, farmers' share in the GDP has been growing steadily, exceeding 10% (Table 1).

Trends in foreign trade of livestock products are also ambiguous. In particular, in 2004-2012, the export under "Live animals and animal products" substantially increased, but import growth rates were also much higher. During this period, Ukraine has transformed into one of the largest exporters of crops in the world.

The livestock structure production has undergone significant transformations in 2004-2012. During that time, the quantity of poultry was increasing, while the quantity of cattle was substantially decreasing.

This trend is indicative not only in terms of demand for the agricultural sector production, but it indirectly characterizes the conditions of production in the separate sectors. The majority of cattle is kept in households (up to 66%), whereas poultry is kept on large farms that belong to agricultural holdings.

In several categories, Ukraine is not able to provide domestic demand for livestock production. Thus, the index of adequacy of food consumption by the group "Meat and meat products" is 0, 62 respectively; by the group "Milk and milk products" - 0, 56 is respectively. These negative tendencies, combined with the fact that in since 1990 cattle quantity in Ukraine has decreased 5.1 times, and the quantity of sheep and goats - in 5.05 times. After a long decline, poultry quantity since 2001 is substantially growing (Table 2).

Dynamics of the world food market also significantly influences the domestic market. In particular, between 2004 and 2010 there was a relentless rise in prices for livestock products (Table 3).

Such price trends facilitate investments in the agricultural sector of Ukraine's economy. However, considerable investment resources are directed into the production of crops, where the production cycle is much shorter and profitability is higher.

In particular, the profitability level of agricultural crop production is 26, 0%, but in livestock it is only 8%. In livestock, investment resources are directed mostly in the development of large poultry farms.

Providing agricultural production remains at an unsatisfactory level: in livestock this indicator is 14.7% of the regulatory requirements, while in crop - 14.3%. One of the reasons of poor livestock development in Ukraine is a lack effectiveness of risk management system.

**Table 1** The role of agriculture production in Ukraine's economy

Indicator	Years								
	2004	2005	2006	2007	2008	2009	2010	2011	2012
The share of agriculture in production of gross value added, %	11.9	10.43	8.64	7.46	7.1	8.25	8.66	9.48	10.4
Export of live animals and animal products, millions of USD	648.48	732.22	396.47	747.15	783.40	595.96	771.38	936.60	961.32
Import of live animals and animal products, millions of USD	314.98	499.64	649.04	771.41	1702.01	1267.55	1241.69	1035.37	1718.37

**Table 2** Indicators of livestock development in Ukraine

Livestock and poultry quantity	Years								
	2004	2005	2006	2007	2008	2009	2010	2011	2012
Cattle (thousands)	7712.1	6902.9	6514.1	6175.4	5490.9	5079.0	4826.7	4494.4	4425.8
Sheep and goats (thousands)	1858.8	1754.5	1629.5	1617.2	1678.6	1726.9	1832.5	1731.7	1739.4
Poultry (millions)	142.4	152.8	162.0	166.5	169.3	177.6	191.4	203.8	200.8

**Table 3** Average realization prices of agriculture production in Ukraine

Price of agriculture production (USD/ton)	Years								
	2004	2005	2006	2007	2008	2009	2010	2011	2012
Livestock and poultry (live weight)	957.27	1348.35	1249.05	1280.49	1933.53	1330.07	1360.59	1501.98	1684.01
Milk and milk products	157.01	219.89	211.92	328.83	392.06	392.06	370.31	381.74	333.14

In our view, the current negative trends in the development of risk management in livestock can be explained by the influence of the following factors:

Historically, revival of the agricultural sector in independent Ukraine was much faster in crop than in livestock. Besides, economical return on investment is much longer in livestock. As a result, demand for agricultural insurance in Ukraine was formed disproportionately toward with crop producers.

Long absence of demand for insurance risks in livestock led to the formation of certain stereotypes in the insurance market of Ukraine among insurers, resulting in little attractiveness of this direction, which negatively reflected on the quality of existing insurance products.

The state directs most of its support at crops, while international experience shows that the role of the state in livestock production and insurance is extremely high.

Throughout all the period of formation, agricultural sector in Ukraine had a great state support. Such an exalted position is recognition of the place and role of agriculture in Ukrainian economics. At the same time, the efficiency of state support of agriculture is still very low. On the current stage the state uses the following instruments of agricultural production's support:

1. Price regulation is provided mostly through interventions of Agricultural Fund on certain commodity markets, as well as through the establishment of minimal purchase prices for certain agricultural products.

2. Various subsidies and grants for producers: for example for the maintenance of cattle. Use of these instruments provides financing from central funds. That is why such support depends on the current state of public finances. Unfortunately, Ukraine has liabilities to the World Trade Organization concerning the restriction of direct forms of agriculture support.

3. Special tax regime for agricultural producers who are paying the fixed agricultural tax and thus exempt from certain taxes and have significant benefits for value-added tax.

4. Payments that are connected with the part compensation of paid interests by the credits and lease payments.

5. A policy of reimbursement of losses to certain agricultural producers who suffered as a result of various environmental and technological cataclysms. The result is the underdevelopment of insurance services for the agricultural sector subjects. It creates some compensational mechanisms which give the opportunity for central funds to reduce financial losses from adverse natural conditions.

6. Subsidies for payment of the part of insurance premiums for contracts concluded by farmers with insurers.

Note that active steps towards the development of Ukrainian agricultural insurance model were made in 2012. During this period, a law was passed called " On peculiarities of agricultural production insurance with state support" which provides state support for insurance of:

Harvest crops.

Harvest perennial crops.

Livestock, poultry, rabbits, fur-bearing animals, bee colonies, fish and other aquatic resources and livestock production.

However, realization of agricultural risk insurance with state support can be made only by those insurers who will be members of a special union the Agricultural insurance pool. This system in Ukraine was realized by analysis of its effective use in other countries that were making agricultural reforms. However, at the current time only 10-12 insurance companies are interested in the realization of agricultural insurance, while there are more than 440 operating in the Ukrainian insurance market. How effective will be this model of livestock insurance in Ukraine? Some potential threats can be identified at the earliest stages, threats connected with the following factors:

The size of compensations for the paid insurance premiums will be reviewed every year, thus enhancing the influence of macroeconomical factors on the development of agricultural insurance. For example in 2005-2008, compensation for the lowering of insurance premiums, which included costs for insurance in the value of agricultural production, was complicated because of bureaucratic procedures. In 2009-2012, such compensational payments were not made. Considering the existing proportions in the dividing of animals between the households and large associations, the given mechanism of compensations does not solve the problems connected with access to insurance services for small holders.

The probability remains for significant influence from state bodies, as in the activity of the Agricultural insurance pool on the allocation of funds for compensation.

The factual absence of data about livestock insurance over the period 1991-2012 significantly complicates the evaluation of risks in the first periods of the Agricultural insurance pool activity.

Widening of insurance services in Ukraine is mostly dependent upon the increasing of efficiency management in this area - primarily at the level of households versus on the level of large subjects.

At the same time, it is necessary, for the individual risks of households, to forecast when certain insurance events happen with animals, and compensation of premiums for concluded insurance contracts.

## CONCLUSION

The realization of livestock's development strategy in Ukraine determines the necessity of creation of effective insurance protection system for participants of agricultural market. Nowadays livestock insurance in Ukraine is used very limited, even in comparison with crop insurance. This

significantly reduces the impact of economic activity in livestock. An important factor in the expansion of livestock insurance should be a change in priorities in the state policy for the agriculture sector support. Widening of insurance in Ukraine's agricultural sector is, largely, due to the active implementation of international experience, especially of economically-developed countries. In our view, such an approach is not always justified, because states' opportunities differ significantly concerning the financing of particular directions and oversight of participants of agricultural insurance market. The current state of public finances in Ukraine significantly reduces the opportunities of effective realization mechanisms for reimbursement of insurance premiums, which are approved by legislation. Besides, the majority of livestock production in Ukraine is in individual households that do not have necessary resources and experience to conclude insurance contracts. It is necessary to provide conditions for the active interaction of demand and supply for insurance services in livestock, especially considering the size and peculiarities of producers' financial position. It is important to use the experience of those countries that provide access to livestock insurance for small farms and for large groups. In such conditions, the livestock insurance will cover a large quantity of agricultural sector producers, allowing Ukraine to gain sustainable competitive position in the global market of agricultural production.

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