



INSTITUTE OF AGRICULTURAL  
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# The Common Agricultural Policy of the European Union – the present and the future

Non-EU Member States  
point of view

74.1

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INSTITUTE OF AGRICULTURAL  
AND FOOD ECONOMICS  
NATIONAL RESEARCH INSTITUTE

**The Common Agricultural Policy  
of the European Union –  
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**Non-EU Member States  
point of view**

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CHALLENGES, CHANCES, THREATS, PROPOSALS**

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The publication is a collection of selected papers delivered at the 22th edition of the International Scientific Conference organized by the Institute of Agricultural and Food Economics - National Research Institute. The theme of the conference was "The Common Agricultural Policy of the European Union – the present and the future. The conference was placed on 5-7 December 2017 in Stary Jablonki in Poland. Common Agricultural Policy was and still is one of the key pillars of European integration. Published in two volumes materials refer directly to the current and future of the CAP in EU and non EU member states, the strategic objectives and principles of agricultural policy for the agri-food sector and rural areas, address the issues of equilibrium between agriculture, forestry and land use, relate to the dilemmas for the EU budget and the CAP after 2020, CAP instruments and their adjustment, transformations of the rural economy and programming of the rural and agricultural policy, as well as productivity and production efficiency and tensions between sectoral action and between different models of territorial activities.

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# Contents

Introduction .....	7
1 Urban agriculture: a framework for agricultural policy – present and future .....	15
<i>Prof. Drago Cvijanović, Prof. Otilija Sedlak, Ph.D. Željko Vojinović</i>	
1.1. Introduction .....	16
1.2. Advantages of urban agriculture .....	17
1.3. "Smart Cities" .....	18
1.4. Manifestations of Urban Agriculture.....	21
1.5. Challenges of Urban Agriculture.....	23
1.6. Conclusion.....	24
References .....	25
2 Land market and a village-keeping model of the agrarian system of Ukraine.....	27
<i>Dr Iurii Lupenko, Dr Valerii Zhuk</i>	
2.1. Introduction .....	27
2.2. Analysis of recent research and publications .....	28
2.3. The main results of the study.....	30
2.4. Summary and conclusions.....	36
References .....	37
3 Agrarian policy in the European Union and financial support to Serbia.....	38
<i>PhD Biljana Grujić, PhD Predrag Vulović</i>	
3.1. Introduction .....	38
3.2. Agrarian policy in the EU .....	39
3.3. EU Agrarian Policy towards Serbia .....	44
3.4. Summary and conclusions.....	53
References .....	54
4 Ukrainian agricultural market regulation tools: their effectiveness and directions of improvement.....	56
<i>Prof. Olga Varchenko</i>	
4.1. Introduction .....	56
4.2. Data and Methods.....	57
4.3. Results and Discussion.....	57
4.4. Summary and conclusions.....	69
References .....	69

5	The Common Agricultural Policy of the European Union and the ways of its implementation in Ukraine .....	71
	<i>Dr Vasyl D. Zalizko, Prof. Nataliia M. Vdovenko, PhD Violeta L. Heraimovych, Assoc. Prof.</i>	
5.1.	Introduction .....	71
5.2.	The evolution of the EU Common agricultural policy .....	72
5.3.	New priorities of the European Union for 2014-2020: strategic directions for Ukraine's agricultural sphere development .....	74
5.4.	Organic component of the agricultural policy of Ukraine and common agricultural policy of the EU .....	75
5.5.	Summary and conclusions .....	79
	References .....	80
6	Farm's financing patterns and financial system development: evidence from Ukraine and Poland .....	81
	<i>Prof. Olena Oliynyk-Dunn, Prof. Viktor Adamenko</i>	
6.1.	Introduction .....	81
6.2.	Research methods .....	83
6.3.	Results .....	84
6.4.	Summary and conclusions .....	95
	References .....	96
7	The moratorium on agricultural land sale as a limiting factor for rural development .....	97
	<i>Prof. Anatoliy Danylenko, PhD Tetyana Sokolska, PhD Olena Shust</i>	
7.1.	Introduction .....	98
7.2.	The main results of research .....	99
7.3.	Summary and conclusions .....	110
	References .....	112
8	Solutions to the problems of rural territories development as a sign of their positive brand .....	114
	<i>Prof. Oleksandr Pavlov, Iryna Pavlova</i>	
8.1.	Introduction .....	114
8.2.	Problems of rural territories development .....	117
8.3.	Branding as a marketing tool for solving the problems of rural territories development .....	124
8.4.	Brand of rural territories development in Ukraine .....	127
8.5.	Summary and conclusions .....	131
	References .....	132
	Instead of a summary .....	133
	Annex I .....	135

## 5 The Common Agricultural Policy of the European Union and the ways of its implementation in Ukraine

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### **Abstract**

The new economic policy in Ukraine implies the use of the benefits of the free trade regime with the European Union member states. To improve the competitiveness of domestic agricultural products, it is expedient to use the experience of European Union, which has gone a long way to its formation. Common agricultural policy of EU member states was ensured through effective mechanisms. Mechanisms that create cross-responsibility - from producers: high quality products, maintenance of land in a proper condition, and on the part of the state – guarantees of subsidies and financial support. This experience should be used to form an effective Ukrainian agricultural market.

**Keywords:** European Union, agricultural market Common agricultural policy, competitiveness, subsidies, agroindustrial complex.

**JEL codes:** F36, F37, Q12, Q18

### **5.1. Introduction**

The following scientists were engaged in the study of the agro-industrial complex and the common agricultural policy of the EU: Duhienko N., Vinichenko I., Omeliyanenko T., Bazylevych V., Kovalchuk S. and others,

however, not all aspects are sufficiently studied and reflected, which makes further research necessary and relevant.

The goal of the study is to analyze the common agricultural policy of the EU, to systematize its main stages and principles, and to formulate effective mechanisms that will contribute to the development of Ukrainian agricultural market.

## **5.2. The evolution of the EU Common agricultural policy**

For the first time, the Common Agricultural Policy (CAP) was introduced in the countries of Western Europe in the 50's of the 20th century. At that time, due to the war, it was impossible to provide sufficient amount of food, since Europe's agriculture was destroyed. Therefore, the first goal of CAP was to ensure high labor productivity throughout the entire food production chain and to provide the EU with a viable agricultural sector of the economy. The CAP encouraged the production of agricultural products by way of paying farmers and guaranteeing high sales prices for them. Financial support was provided to expand production, to introduce new technologies. It helped farms survive and develop. Although the CAP was very successful in moving the EU towards self-sufficiency, by the 1980s the EU had to contend with almost permanent surpluses of the major farm commodities, some of which were exported (with the help of subsidies), while others had to be stored or disposed of within the EU. These measures had a high budgetary cost, distorted some world markets, did not always serve the best interests of farmers and became unpopular with consumers and taxpayers. At the same time society became increasingly concerned about the environmental sustainability of agriculture.

The 1992 reform started the process of reduction in support prices and the introduction of direct payments for a few key agricultural sectors. A new set of reforms initiated in 2003 and continued in 2008 with the Health Check, aimed at enhancing the competitiveness of the farm sector, promoting a market-oriented, sustainable agriculture and strengthening rural development policy. A central element of the latter reforms was to 'decouple' the majority of direct payments from production. That is, farmers were no longer to receive payments related to a specific type of production. Instead, payments were linked to entitlements based on the value of historical subsidy receipts, conditioned to the provision of environmental public goods. In parallel, a comprehensive rural development policy was introduced as Pillar II of the CAP; this policy encouraged many rural initiatives while also helping farmers to diversify, to improve their product marketing and to otherwise restructure their businesses. The recent OECD evaluation of CAP reform confirmed that this reform process led to a significant

decrease in the distortion of production and trade and an increase of income transfer efficiency. Measuring the amount and type of support to producers using the OECD Producer Support Estimate (PSE) indicator, the share of potentially most distorting support in PSE decreased from 92% to 34% between 1986-88 and 2007-09; it is projected to further decrease to 27% when the Health Check reform is completed. The share of gross farm receipts derived from support to producers decreased from 39% to 23% between 1986-88 and 2007-2009, close to the OECD average of 22% in 2007-09.

At the next stage of CAP (2007-2013) the following priorities were set:

- strengthening competitiveness of agriculture. To achieve this, restructuring and modernization of the agrarian sector were foreseen; support for integration links; access to scientific and technical achievements and support of their implementation; access to the information and introduction of information technologies; support for the production of new agricultural products; support of producers cooperation;
- environmental protection in the countryside. State support was focused on the introduction of energy-saving technologies; preservation of natural resources; reduction of the harmful agricultural climate impact;
- improvement of life quality in rural areas and stimulation of non-agricultural employment.

State support was also needed for the development of small businesses and crafts in rural areas; tourism development; development of education for the needs of the rural economy; modernization of rural infrastructure; creation of the system for innovative use of renewable energy sources derived from agricultural products, etc. At the fifth stage, basing on the analysis results, the requirement for farmers to keep 10% of their arable land set aside was cancelled; a decision was made to gradually increase milk quotas and to eliminate them in 2015. A decision was made that surplus products will only be purchased by the governments to protect the market and growers income, when commodity prices drop below a dangerously low level.



### 5.3. New priorities of the European Union for 2014-2020: strategic directions for Ukraine's agricultural sphere development

For the period 2014-2020, the goals and objectives of the CAP were identified basing on discussion held with the participation of representatives of European environmental organizations and farmers, consumer and animal rights protection organizations, transnational companies and the European Commission among others. The decision-making process was different from previous reforms, for the first time the European Parliament was only a co-author of the reforms. The main goals of the modern stage of the CAP:

- viable food production;
- sustainable management of natural resources and climate;
- actions for balanced development of the territories.

The peculiarity of the current stage of CAP is to focus on the provision of public and private benefits as a result of its implementation. Farmers should be rewarded for services they provide to the broad public, such as landscapes, biodiversity of agricultural land, even if they do not have market value. Thus, the goals of the new policy have two levels. The first level is the provision of environmental public benefits. The second level, a regional one, should complement first international level, given the wide variety of agriculture, production potential, environmental as well as socio-economic conditions and needs in the EU. Both levels are framed by clearly defined budget constraints, in order to ensure equal conditions at European level aimed at achieving common goals. EU countries are jointly responsible for balancing potential benefits and costs for both producers and national authorities. In order to achieve the set goals, measures have been taken to adapt the methods of CAP.

Thus, increasing the competitiveness of agriculture is achieved through the introduction of changes in the market mechanisms interference tools, in particular the abolition of 312 production restrictions. All existing restrictions on production volumes for sugar, dairy products and wine will be eliminated, which will allow farmers to amend production in response to world demand growth. Dairy quotas will expire in 2015, quotas for sugar – in 2017, and in the wine industry – in 2018. Regulatory measures should also enhance agriculture competitiveness: an enhanced legal framework extends the possibility for collective bargains (in some sectors) and supply contracts (for all sectors), and introduces a temporary exemptions from certain rules of competition during the periods of market imbalance.

Another tool that strengthens competitiveness at a farm level is young farmers support. This tool was introduced because the EU countries faced with the aging of the rural population (only 14% of EU farmers are aged under 40 years). From 2015, all young farmers entering the sector are able to receive an additional subsidy.

These tools are designed to help the agricultural sector adapt to the new trends and technologies, thus becoming more effective. The new CAP also offers tools that enhance the EU's ability to manage crises. The crisis fund, which counts 400 million euros per year in 2011 prices, was created. Its financial resources are planned to be spent in the event of a crisis, the source of fund filling – deductions from direct payments. Unused amounts are planned to be reimbursed to farmers in subsequent budget years. Other risk management tools are also offered: insurance for crops, animals and plants, as well as mutual funds and an income stabilization tool. Agriculture have to improve environmental efficiency through more sustainable production techniques. In order to receive full financing under the CAP the farmers have to comply with the mandatory basic ecological requirements and obligations, which will allow to achieve this goal. Also, from 2015, a new direct payment policy tool is introduced: 30% of national direct payments goes to farmers for meeting the three mandatory agricultural practices: keeping sustained pastures, environmental focus areas and diversification of crops. Based on these methods, rural territories development will play a key role in achieving the environmental goals of the CAP and in combating climate change. Also, at least 30% of the budget of each rural development program should be reserved for measures beneficial to the environment. These include agro-climatic events, organic agriculture, etc. All these activities make a significant contribution to the improvement of the environment, because they are adapted to the local needs. The entire set of complementary policy tools is accompanied by appropriate training and other maintenance from the Advisory Institutions.

#### **5.4. Organic component of the agricultural policy of Ukraine and common agricultural policy of the EU**

So-called environmentalization and organic production are among the key positions in the new program period of 2014-2020. Stimulation of environmentalization of agriculture within the framework of the CAP is provided through “green payments” - compensations for the maintenance of pastures, conservation of environmental areas (up to 7%), conservation of biodiversity and natural landscapes. To help farms to solve problems related to the quality of soil and water, climate change, about 30% of the budget of the

rural territories development program should be allocated for agro-ecological measures, support for organic agriculture and projects related to innovations or environmental investments in this area. Subsidies for these purposes are set proportionally to the area of arable land without fixing the upper limit of payments to farmers. CAP strategy till 2020 supports organic producers.

Today, large-scale agribusinesses account for 51% of the gross domestic product of agribusiness in the EU, the remaining 49% are farms. Thus, the strategy is to keep the equal opportunity for small and medium-sized farmers and cooperatives to enter domestic and local markets along with largescale agrarian companies, to protect their income from market and natural factors. In the new program period 2014-2020 compared to the previous period (2007-2013), the share of CAP in the EU budget drops from 39% in 2013 to 33% in 2020.

Priority also remains to be given to local resources used for ecosystem conservation and climate change risk prevention. Financing of preferential sales of organic products and the development of partner relations between processing enterprises, protection of rights of agricultural non-governmental organizations is increasing. In addition, the amount of direct compensation to farmers is changed depending on the recipient country: for old members these payments are reduced by 5% (from 282 euros/hectare to 269 euros/hectare), and for new members of the EU they increase by 60%. In the context of the European integration of Ukraine, the growing factor for increasing the competitiveness of the economy is the production of environmentally friendly (organic) products. Production of organic products is officially defined in Ukraine as a priority of the state support. The Strategy for Ukraine's Agriculture Development "3 + 5" developed by the Ministry of Agrarian Policy and Food suggests the following directions of the reform: stimulation of organic production, expansion of markets for agricultural products, development of rural territories, irrigation of land and food safety.

In particular, the Ministry and the State Geocadaster are developing a mechanism to stimulate the production of organic products through the special land auctions. They assume that the market operators will be offered land plots at preferential rental rates to place organic production. Preferences will only come to force from the moment of actual implementation of the investment project – the beginning of the certification process, which means confirmed fixed intentions. In case the stated auction conditions are not observed by the auction winner the rental rates applied will be returned to the market level – the average in the corresponding area. Today, foreign partners are interested to cooperate with Ukraine by way of purchasing organic raw commodities, rather than the ready to eat food product, which shifts the emphasis of this cooperation

towards the raw commodities market share. This is primarily due to the lack of effective legislation, and hence the mechanism for regulating the organic products market and the corresponding control system. Such conditions create a favourable environment for the consumer rights abuse and the development of unfair competition among producers. That is why, according to specialists, the Rada of Ukraine should adopt the draft Law "About Basic Principles and Requirements for Organic Production, Circulation and Marking of Organic Products" and regulatory bills for its implementation.

Having considerable potential for the production of organic agricultural products, their exports and domestic consumption, Ukraine has achieved some results in developing its own organic production. So, the area of certified agricultural land engaged in the cultivation of various organic products in Ukraine already exceeds four hundred thousand hectares, and our country holds the honourable twentieth place in the chart of world organic movement leaders. The share of certified organic areas among the total agricultural land in Ukraine is about 1%.

In this context, it should be noted that the lack of a network of domestic certification companies is a serious slowdown in the development of organic production in Ukraine. To date, Ukraine has only one domestic certification body (Organic Standard), which sets the high prices for certification and small and medium-sized agricultural enterprises do not have the financial capacity to undergo organic certification.

At the same time, Ukraine is a leader among Eastern European region in terms of the certified area of organic arable land, specializing mainly in the production of cereals, leguminous and oilseeds. Official IFOAM statistical surveys confirm that in 2002 there were 31 registered organic farms in Ukraine, while in 2016 there were already 360 certified organic farms, and the total area of certified organic agricultural land calculated 411,200 hectares. Studies of the Organic Movement Federation of Ukraine show that domestic consumer market for organic products in Ukraine began to develop from the beginning of the 2000s, amounting to: 2006 – 400 thousand euros, 2007 – 500 thousand euros, 2008 – 600 thousand euros, 2009 – 1.2 million euros, 2010 – 2.4 million euros, in 2011 this figure increased to 5.1 million euros, in 2012 – to 7.9 million euros, in 2013 – up to 12.2 million euros, in 2014 to 14.5 million euros, in 2015 – to 17.5 million euros, and in 2016 – to 21.2 million euros [Berlach, 2009].

In order to determine the importance of the organic sector in agricultural production, it is worth pointing out the rapid pace of development of this sector. For this we calculate the forecast, that describes the dynamics of organic production in Ukraine based on the theory of approximation, which requires the

construction of spline (coconvex polynomial of degree 2) and you must define the Finite differences of k-th order. In the role of approximant we use the quadratic coconvex spline L for which inequality is proved

$$|f - L| \leq c\omega_3(f; \rho_n),$$

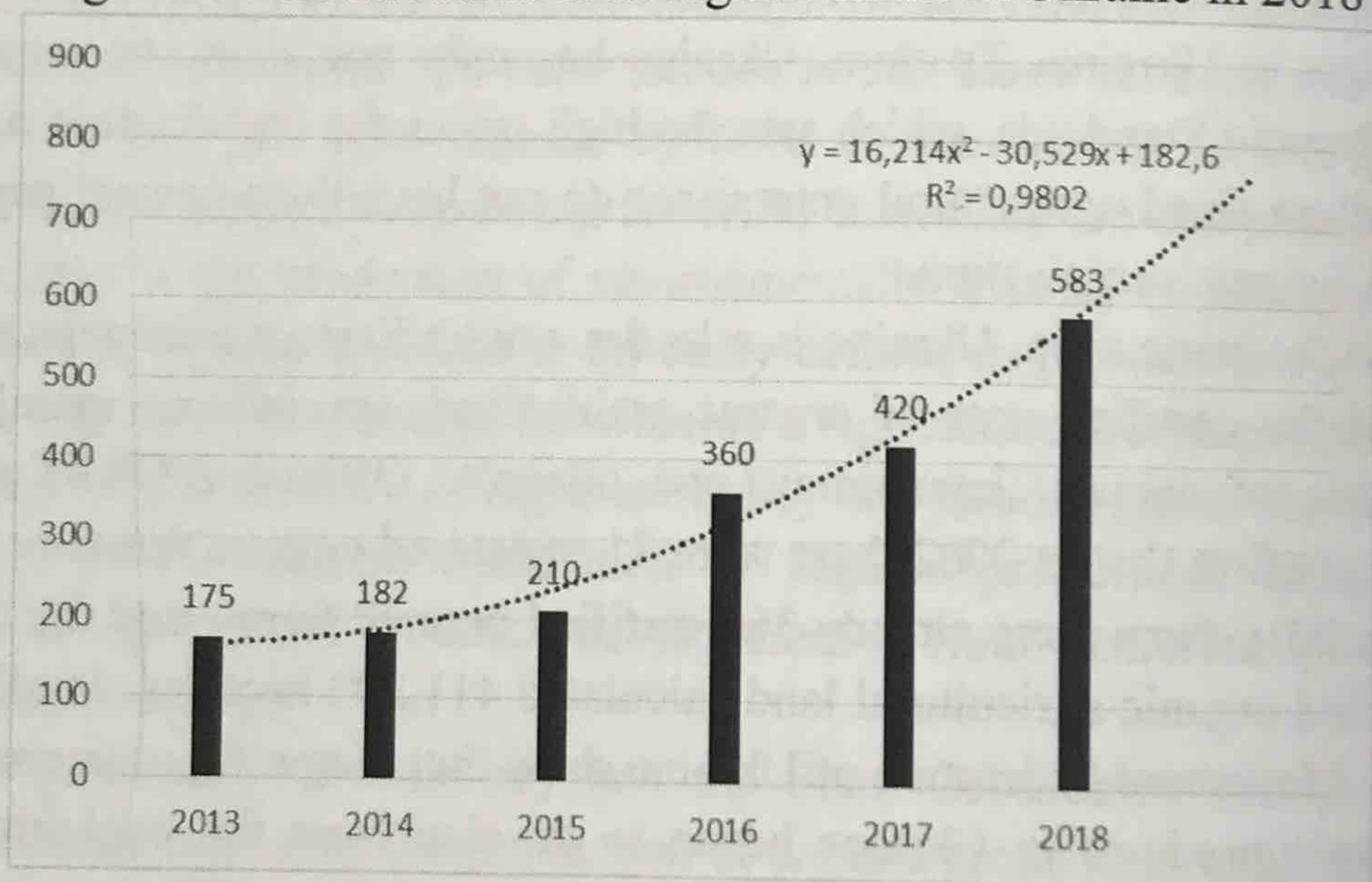
$$\rho_n = \frac{1}{n^2} + \frac{(1-x^2)^{1/2}}{n}, n \in \mathbb{N}, x \in [a, b], a > b,$$

(1)

where  $f$  – a certain function given by the tabular method,  $c$  – constant, which depends on the choice of the points of the partition (years),  $\omega_3(f; \rho_n)$  – the modulus of continuity (smoothness) of the third order, which is calculated using the mathematical tool Wolfram Mathematica 10 (details see, for example, [Zalizko and V. I. Martynenkov, 2016]).

Thus, the short-term forecast for the development of the organic market of Ukraine for 2018 indicates an substantial increase of organic market (Fig. 1).

Figure 1. Forecast number of organic farms in Ukraine in 2018



Source: author's calculations and presentation based on the data of the State Statistics Service of Ukraine

It should be noted that an increase in the number of certified producers will contribute to filling the domestic market with its own organic products by adjusting domestic processing of organic raw materials. For comparison, in 2014 there were about 260 thousand organic producers in the EU (340 thousand in Europe). The largest number in Italy - nearly 49 thousand and Turkey - 71 thousand. According to IFOAM, since 1999, the number of organic producers

has increased 10-fold to 2.3 million. More than 75% of all manufacturers are located in Asia, Africa and Latin America. Diagnosis of the current state of the domestic organic agri-food market has shown that the indicators of its functioning are increasing, but still they do not correspond to the level of highly developed countries. In order to ensure its effective development in the future, it is necessary to deploy a complex program for decisions and actions aimed at increasing the profitability of domestic production structures and infrastructure of this market.

Organic production plays an important social, economic and environmental role for the whole country. Organic production technologies are aimed at improving the ecological conditions, improving the quality of soils, preserving biodiversity (Zalizko et al. 2017). A positive effect shows itself also as increase of the competitiveness of Ukrainian products on the world markets, therefore the development of organic production and organic products market should become one of the priority directions of the state policy in the agricultural sector. The main task of the state in modern conditions is to maintain positive trends in the organic market of Ukraine. The adoption of the Law "About Basic Principles and Requirements for Organic Production, Circulation and Marking of Organic Products" should become an effective step in this direction, in line with the requirements and principles of organic production regulation in the EU, and the relevant regulatory bills for its implementation.

## **5.5. Summary and conclusions**

The value of the Common Agricultural Policy is the possibility to open new prospects for the formulation and implementation of a transparent agricultural policy in our country. Over the years of independence, Ukraine's agrarian sector has become the most discussed and remains one of the priorities even in the worst times. However, a number of programs aimed at the revival of the Ukrainian village, the development of cooperatives, small and medium farms did not have the desired effect. CAP stands for a constructive dialogue between the authorities, the producer and the consumer, for an open and transparent agricultural policy.

Given the Ukrainian organic market forecast in the conditions of shrinkage of the budget framework (under the influence of the WTO requirements), it is important that resources should be distributed in such a way as to maximize the achievement of the CAP goals. Efficiency increases through the targeted support, fair distribution of subsidies between countries and within member states and a strategic approach to their use. The strategic task of

the CAP remains unchanged, but the current situation on the world markets, WTO agreements on trade liberalization of agricultural products, on the one hand, and the divergence of the agricultural sectors development levels indifferent EU countries, which had historically formed, on the other, make it necessary to review CAP regularly, to improve policy tools and to state new goals. So, under the influence of the trend to step away from direct subsidies and price support, the CAP in the coming years will direct more and more money to measures related to regional development programs, research and infrastructure development. Nevertheless, the policy is absolutely consistent, there are no discrepancies between the strategic goal and the tactical tasks, the policy is characterized as coherent and flexible at the same time.

In contrast to the EU, Ukraine has no clear state agricultural policy, adequate towards contemporary challenges and threats. This factor has a significant negative impact on the competitive position of Ukrainian agricultural sector in the world markets and will aggravate the vulnerability of the agro-industrial complex to both external and internal factors influence. It is, therefore, advisable to take into account the positive experience of the EU member states conducting the CAP.

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