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DISRUPTED INSTITUTIONS AND INVESTMENT CLIMATE IN UKRAINE

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Abstract

Here is a paper that aims to investigate political instability, institutional configuration in Ukraine, strong location advantages and scares presence of Polish or many other FDI in Ukraine. The main problem of this paper is that there is so little evidence for global value chains in Ukraine despite very good location advantages or internalization possibilities. Furthermore, Ukraine have a history of advanced high-tech industry. Is it possible that unsuccessful politics alone was the main reason for FDIs not being present in Ukraine?

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Disrupted institutions and investment climate in Ukraine

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Introduction

This paper is exploratory. Its main purpose is to investigate what impact Free Trade Agreement (FTA) would have on Foreign Direct Investment (FDI) in Ukraine. We chose Ukraine, because of two main reasons. First, (we thought) it was a perfect time to investigate the motives and incentives to enter to FTA from the FDI perspective taking a critical path towards European legal system and common market. And second, that if Ukraine is a country where most of the location-specific advantages and other OLI advantages (Dunning, 2001) could have been easily satisfied, only actual legal aspects holds the country back. There is an evidence for FDI in Ukraine even taking into account a history of unfavorable investment climate and there is also evidence for respective location advantages in Ukraine (Nowak et al, 2014). Also in the past Ukraine was in the core of Union of Soviet Socialist Republics (USSR), what makes it even more interesting because what we have been about to observe was a part of a transformation process. Unfortunately at exact moment when we planned to conduct the core investigation, a strong political instability accrued and might have severely influenced the results of this research. This gave us two choices, we either postpone our investigation or we focus on understanding political and institutional aspects of the investment climate in Ukraine and its impact on FDI using available statistical data.

We have been particularly interested in Polish FDI in Ukraine. Because between two countries there is a ‘geographic and cultural proximity, and a history of special political relations’, but regardless of that “the level of Polish Investment in Ukraine is very modest (…) Polish FDI flows to Ukraine and stock in Ukraine represent only 1-2% of the value of outward FDI from Poland. At the same time, however, the second largest number of Polish investors have established their affiliates in Ukraine. Only Germany hosts more Polish subsidiaries than Ukraine.” (Nowak et al, 2014).

The reason we had to modify our research resulted from a recent (December 2013 – January 2014) actions taken by a former Ukrainian government towards establishment of Free Trade Agreement (FTA) with European Union (EU), followed later by a rejection of the deal, and other developments. We wanted to know how influential this events are for FDI in Ukraine (particularly for Polish and EU FDI). Therefore this paper aims at finding the main determinants that influence Ukrainian Investment Climate, beside strong recent and evident political shocks.

Political instability that have been mentioned above, dates back much further than the failure of FTA and negotiations that were aimed to replace previous ‘agreements for partnership and cooperation’ from 1994. After the initial talks the first stage of the new deal have been reached on 11th of November 2011 in Brussels (during the twentieth round of negotiation) and on the fifteenth EU-Ukraine summit held on 19th December 2011 in Kiev, representatives from Ukraine and EU officially acknowledge the final agreement and the document was ready-to-sign on 30th March 2012 but President Yanukovych did not sign it.

The aim of the new deal was to deepen the cooperation between EU and Ukraine, and to strengthen a cooperation on a multilateral level (Polish Ministry of Foreign Affairs, 2014). The

FTA aimed also to create a strategic point of orientation for systemic socio-economic reforms and for further adaptation of selected EU laws and policies. In other hand it was created to bring Ukraine closer to the EU – fast. At the same time there was a growing economic pressure from Russian Federation which was a strong signal for Ukrainian Government that trade with Russian Federation could be permanently shut if talks with EU would continue. The Trade War between Ukraine and Russia resulted in a gradual reduction of Ukrainian GDP, industrial production, investment and export – what ultimately forced Ukrainian Government to reject the policy leading to agreement with EU.

On 21st of November 2013 which was only days from a summit in Vilnius, Ukrainian Government permanently suspended all actions leading to the agreement what directly lead to protests more powerful than Orange Revolution from 2004. In return Ukrainian Government proposed that all further talks should be continued for a tripartite committee EU-Ukraine-Russia and that the costs arising from decreasing value of trade with Russia should be compensated by the EU.

Another aim of this investigation was to find out what might have gone wrong, and caused a gradual degradation of investment climate and investment opportunities. In the past Ukraine have been known for nuclear power research, advanced aeronautics, rocked science and other intensive R&D activities. At present the country seem to lose its potential to pioneer in areas of General Purpose Technologies (GPT) the same way as it lost to attract more Foreign Direct Investment. In contrast, political stability, favorable investment climate, FDI and knowledge satiation per square meter can produce knowledge-intensive clusters like a silicon valley in the US (Mazzucato, 2013).

Opportunities for GPT in Ukraine

To attract FDI counters usually must show a relatively stable political environment, liberal taxation policy etc. Sometimes to attract FDI countries use special incentives (i.e. special economic zones and CIT reduction). Multinationals are also interested in intellectual property rights crucial for FDI that needs to transfer technology and know-how, patents or trademarks as well as the managerial expertise (Hymer, 1976). Notwithstanding that, FDI that attracted by favorable IP could create various positive spillover effects (Javorcik and Spaterenau, 2005).

Knowledge-intensive FDI usually settle around locations with a well-trained human capital, educated to use complicated machinery. According to Global Competitiveness Rapport (2013) Ukraine ranks 63 among 122 countries in Human Capital Index with education level similar to Malaysia (22), Jordan (52) and Bulgaria (56).

Wilson (2000) states that costs of investments are as important as financing (in the form of grants, bank loans or own resources). There are some other factors consistent with other macroeconomic FDI theories like conditionality, risk-bearing and IP regulations (Hymer, 1976).

Positive outcomes for Ukraine's R&D trajectory might have been based on the Helpman's (1998) idea on GPT's characterized by "three core qualities: 1) they are pervasive in that they spread into many parts, 2) they improve over time and should keep lowering the cost to their users and 3) they make it easier to distribute innovation through the invention and production of new products or processes" (Mazzucatto, 2013; Helpman 1998). The main reason for Ukraine's failure to maintain its R&D capacity is caused by institutional instability induced by overgrown protectionism and corruption.

Factors that determine Polish FDI in Ukraine

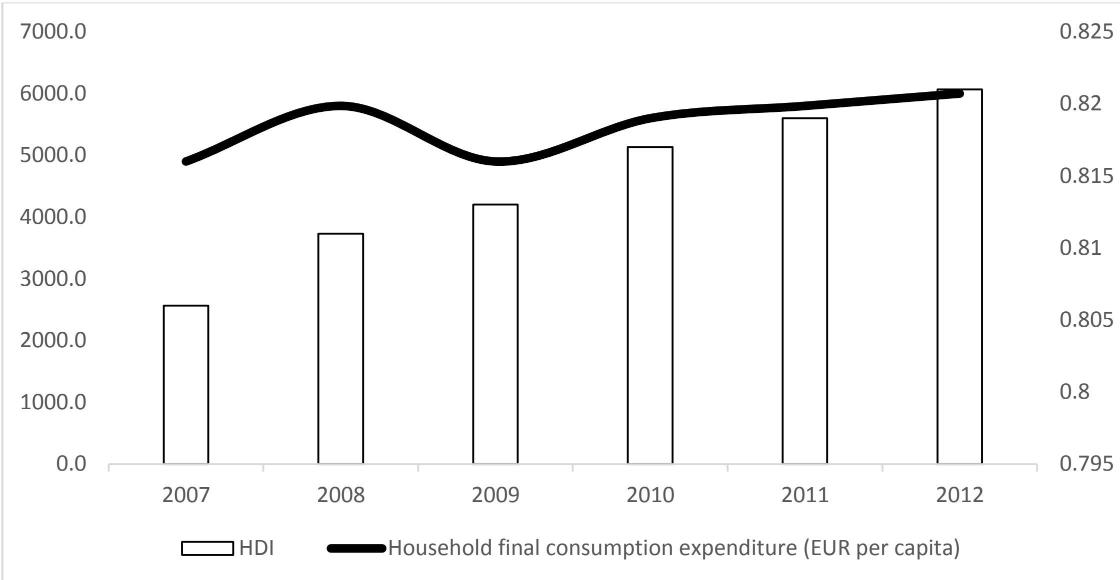
Investment climate reflects many of the characteristics of location advantages. It shapes the potential opportunities and offers incentives to invest. The key word for successfully maintained investment climate is: low risk. In developed economies good investment climate stimulates competitiveness, innovation and sustainable growth. 'Globally, companies that operate in a good investment climate transmit the benefits of low-risk growth on other sectors of the globalizing world' (World Investment Report, 2005).

Looking through the prism of sustainable economic growth, a good investment climate makes investment decisions easier to make, because it creates the environment necessary to maintain undisrupted key activities of the company. Recent events in Ukraine showed a situation where there have been cases of public workers not receiving salary.

Economic and Social Factors

Poland has the largest economy among all post-socialist members of the EU in respect of GDP. The country was a first communist country in Europe, which had officially rejected centrally planned economy – leading off the path for democratic governance in 1989. The period after 1989, have been later followed by reforms introduced by the Finance Minister Leszek Balcerowicz. The reforms opened Polish market to global competition and allowed for price liberalization, reduction of subsidies for state-owned enterprises, initiation of the process of privatization and reform of the banking sector. The period of profound economic reforms and social changes, after the political transformation, is associated with the recession resulting from the rapid structural change of the economy. However, after 1992, the Polish economy recorded a growth well ahead of the other Eastern European countries. In 1994-1997, during the introduction of the "Strategy for the Poland" by Finance Minister Grzegorz Kołotko, Polish GDP was growing on average by 6.4% each year. Next, Poland recorded a stable economic growth with minor declines in 2001 and 2002 (most likely due to the rigorous monetary policy) and in 2009, in response to the global debt crisis.

Figure 1Expenditure of households and HDI in Poland in 2007-2012



Source: Eurostat and UNDP.

In 2007-2012, the consumer expenditures in Poland have been increasing with an average rate of 6.1% a year. The per capita the indicator increased from 4900 EUR in 2007 to 6000 in 2012. Also indicators like Human Development Index (HDI) and consequently GDP per capita, education level and life expectancy promoted Poland for 39th place among all countries surveyed in 2013 by the UNDP (Human Development Reports, 2013). The ratio was increasing on average 0.4% every year during the 2007-2012.

In 2012 in Poland, the rate of innovation and technological progress measured by number of landline subscribers and mobile telephone owners per 100 population showed that a single person holds is approximately 1½ telephone. OECD Index of life satisfaction – part of the "Better Life Index" that aims to capture the standard of living and quality of life: education and safety, housing, income, availability of labour, community and social engagement, the environment, health and balance of private and professional life have been also increasing over the investigated period. As a consequence, when it comes to quality of life Poland ranks at 29th position before Italy, Portugal and Greece, and little after the positions of Japan and South Korea.

Institutional incentives for FDI

Institutional and legal environment is an essential component of the investment climate. This environment is created by values of law and the effects it has on institutions. It shows how government agencies help to facilitate businesses with foreign capital (Przybylska, 2008). Poland was trying to attract FDI, with favourable laws and regulations since the early 90s –

mainly by facilitating safe entry and protection of investment. Polish actions to promote FDI led to the creation of Polish Agency for Information and Foreign Investment (PAIiIZ). Its role was to coordinate promotion and to monitor investment climate for all investments.

During the global economic downturn and despite lower capital flows, the maintenance of economic growth strengthened Poland's position in the rankings as a country of destination for FDI (Zimny, 2012). In 2011, on the scale of 1-5 in which 1 meant very bad and 5 very well 73% of companies indicates that Poland is politically stable and it will be so in the future (Pentor report, 2012). In Poland there are 14 Special Economic Zones (SEZ). After joining the EU, the Polish Government decided to keep SEZ to 2020, later that period was prolonged by six years to 2026 (Cywiński, 2013). Polish SEZ attracted companies like Toyota, General Motors, LG Electronics, Dell and Procter & Gamble (PAIiZ, 2013). The companies located in the SEZ can benefit from many privileges such as CIT reduction and property tax reduction. In addition, companies can receive discount prices for land and free assistance in arranging the necessary formalities.

Capital flows in the form of direct investment

In 2004-2012 Poland received in total 428.8 bln USD of FDI; and during that period each year FDI inflows increased at an average rate of 18.3%. The only exceptions were in 2008 and 2011, when they decreased respectively by -7.9% and -8.1% in relation to the year before. Among all countries which joined the EU in 2004, Poland attracted most of the FDI. Second was Czech Republic – however in 2004-2012, the country received in total 59.9% less of foreign investment than Poland – what shows the gap between the level of investment. Among all countries that joined the EU in 2004, Latvia attracted the least investment (25.3 bln in total). These data however are dependent on the size of the market.

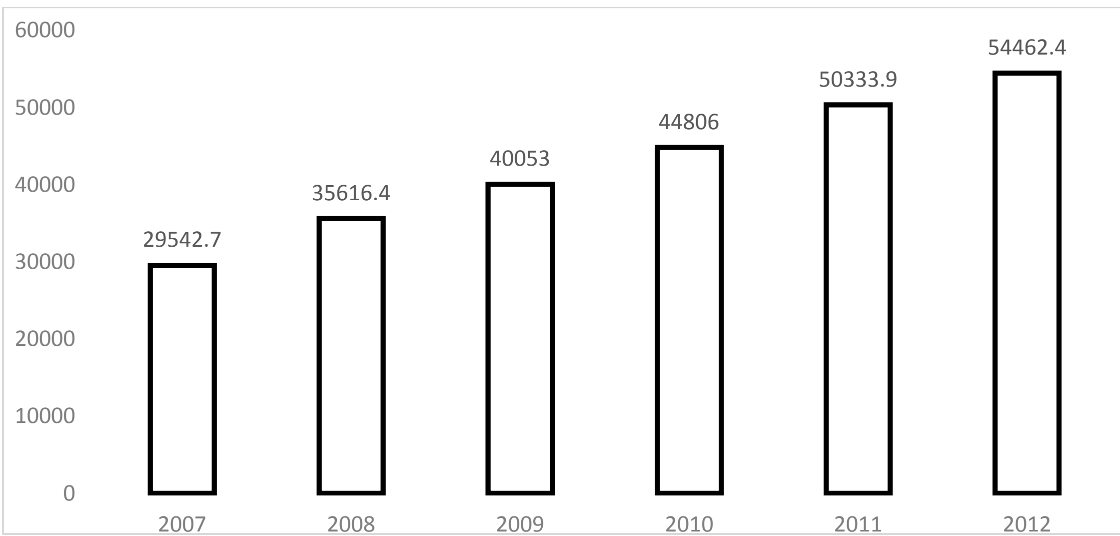
The decline of FDI inflows in 2008 – that is, during the global economic downturn, affected more than half of countries which had joined the EU in 2004. The largest decreases in relation to the preceding year accrued in Lithuania (-14.0%) and Cyprus (-8,4%). The rest of the countries, also recorded a smaller inflow of FDI, but still remained at a slightly higher level than in the previous year. During downturn in 2008 a noticeable amount of FDI went to Slovenia and Slovakia (in relation to the preceding year). These countries recorded inflows of FDI respectively grater by 8.8% and 5.7% in relation to the previous year. However, a year later in Slovenia's FDI decreased by 2.9%. FDI inflows to the new members of the EU in 2010-2011 have been generally decreasing. In 2010, only in Poland and Malta indicated a positive FDI inflows – 16.4% for the Poland and 83.8% for Malta. A year later, the FDI inflows were noted only in Lithuania and Latvia (12.5% and 7.5% in relation to the year before).

FDI and investment climate in Ukraine

Since independence in 1991 Ukraine has been conducting series of institutional reforms. However it is unsure if these actions contributed in positive way to reduce investment risk and costs of business. In fact when it comes to institutional support for business, corruption or bureaucracy Ukraine seem not going forward in relation to other Commonwealth of Independent States (CIS) (Herzfeld and Weiss, 2003).

According to the National Bank of Ukraine (NBU) in 2012, the inflow of foreign capital into the economy of Ukraine reached 7.8 bln USD which is 8.7% more than in 2011. When we compared the first half of 2013 and 2012, the value of foreign capital was lower by 63.4%. The cumulative value of foreign investments in Ukraine at the end of 2012 reached 54.5 bln USD – 79% of cumulative FDI inflows to Ukraine come from EU and 7.8% from other CIS countries.

Figure 2 FDI in Ukraine cumulative in 2000-2013 (* in mln of USD)

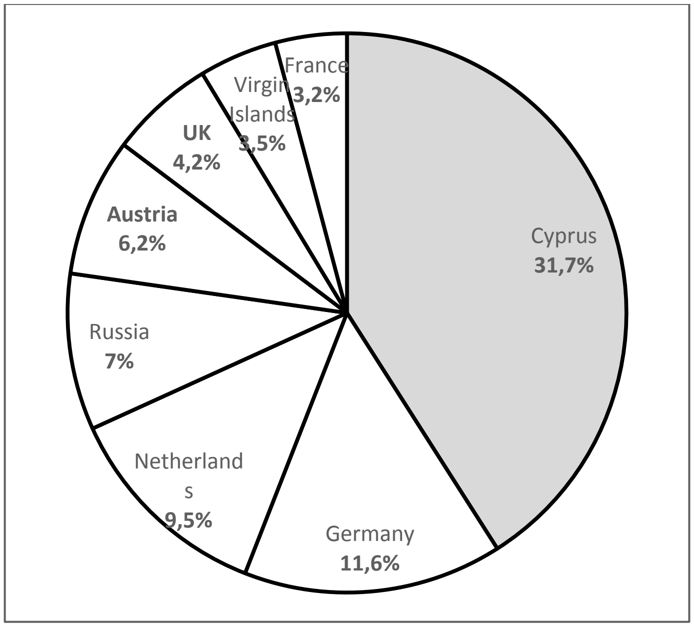


*as of January 1st next year, calculated as the updated value since the start of the investment.

Source: The State Statistics Committee of Ukraine, 2013

According to the data of the State Committee of Statistic in Ukraine (2012), most of the investments to Ukraine comes from Cyprus (31.7%), seconded by Germany (11.6%), Netherlands (9.5%), Russia (7%) and Austria (6.2%). The FDI from Poland did not exceed 1.7% of the total value, (which is roughly the same as from the United States).

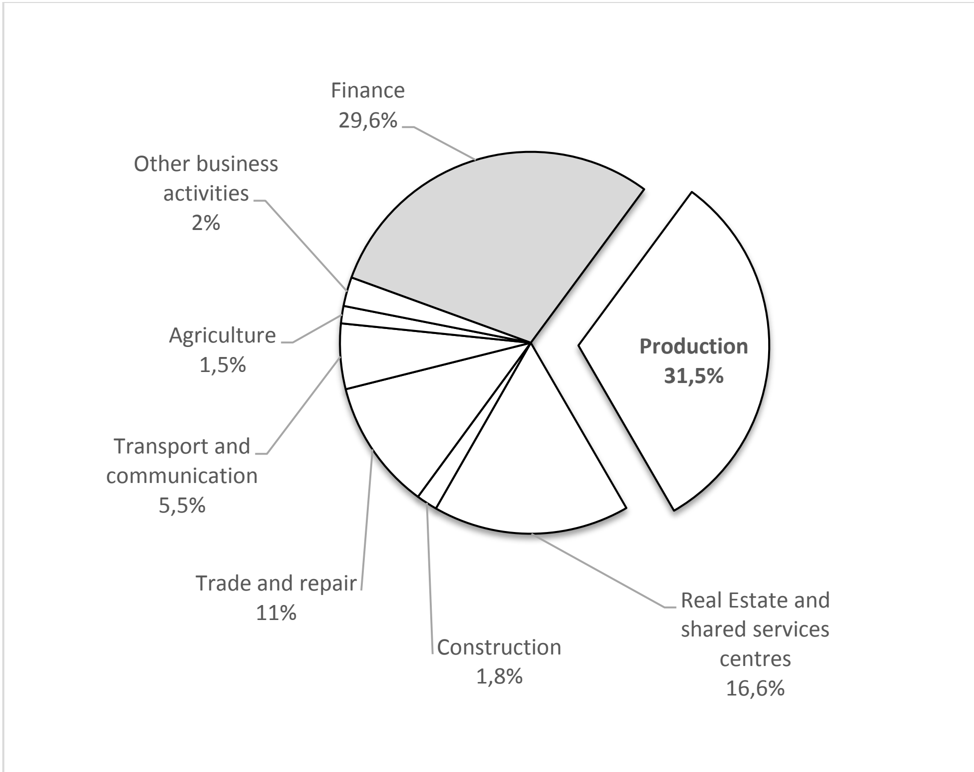
Figure 3 FDI in Ukraine stratification by country's % of total in 2012



Source: The State Statistics Committee of Ukraine, 2012

At the end of 2012 most of the FDI have been directed towards sectors of production (31.5%) –particularly to processing of goods (82% of the total inflow of production). A significant part of the investment have been also located in service sector, mostly in finance (29.6%), real estate and shared services centres (16.6%) or trade and repair (11,0%). Most of the Ukrainian banking have been acquired by mergers and acquisitions in 2006-2007 mainly from EU countries. This kind of investments have been popular in Dnipropetrovsk, Kharkiv districts and the city of Kiev (please see the table below).

Figure 4 FDI inflow to Ukraine by industry in 2012, (in mln of USD)



Source: The State Statistics Committee of Ukraine, 2012

The substantial amount of Ukraine's FDI have been done with tax havens – mainly with Cyprus. Ukrainian capital was often reinvested back in the form of FDI from Ukrainian-owned Cyprus companies. This was done to benefit from advantageous regime tax of Cyprus. What is more investments coming from the Cyprus might also carry capital from Russian M&As. There is no concrete data on Ukrainian financial investments in Switzerland, United States or other countries as there is a significant involvement of third countries – what makes them hard to trace statistically.

FDI inflows to Ukraine are relatively low. Countries the size of Ukraine are usually able to attract much more FDI (Nowak et al, 2014). One of main reasons is a very bad investment climate. There might be a negative correlation between investment in Ukraine, measured risk factors and Brownfield –Greenfield – M&A strategies. Further investigation is needed, however we have encountered a problem collecting relevant data from State Statistics Committee of Ukraine to conduct it. Also the preliminary investigation showed that Special Economic Zones and similar institutions have been playing a very marginal role in attracting FDI in Ukraine. The main reason for low effectiveness of institutionalized help is related to (too) quickly changing tax policy. SSE in Ukraine attracted circa 600 mil of USD which is only 7.2% of the total amount of FDI in Ukraine, but some of them have been windrowing due to mentioned negative taxation policy related to a growing Government budget imbalance.

Risk factors in Ukraine are critical. The Heritage Foundation in the annual Economic Freedom Index in 2012 positioned Ukraine on 161 place among 183 research countries. In 2013 Ukraine was still on the same place – the lowest score among all countries from European Continent. This puts Ukraine with the group of countries with a repressive attitude towards business. In previous years, the Economic Freedom Index has been fluctuating or improving by 0.1-0.2 points, however the late changes are negative. What is more when we compared Ukraine's score in the Index with neighbouring countries', we could draw the line separating Belarus (154 position) and Russia (139) from Poland (57), Czech Republic (29) and Turkey (69)(The Heritage Foundation, 2013).

Other reports also confirmed high risk level of business. Doing business index in 2013 positioned Ukraine on 137/185 place (World Bank, 2014). Numerous of other data and press releases also indicated a bad investment climate. For instance, to start a business in Ukraine, you need to overcome approximately 10 complicated procedures, which is almost twice more than in OECD countries or Western Europe. The whole process of setting up a business also takes twice as long as in the above-mentioned countries. The situation is similar in the case of construction time or property registration. What is more it is hard to credit the initial stage of the project. Many of the difficulties, that entrepreneurs have to face up comes from the fiscal system. Closing the business in Ukraine is also much more expensive and time-consuming than in other European countries.

Despite the existence of the high level risk associated with doing business, Ukrainian economy is still an attractive place to invest and the country manages to attract FDI. At the end of 2012 it was more than 130 countries interested in investing in Ukraine. The value of FDI in the Ukraine's economy at the end of 2012 was 54,5 bln USD (Ukrastat, 2013).

Polish FDI in Ukraine diagnosis for 2000-2012

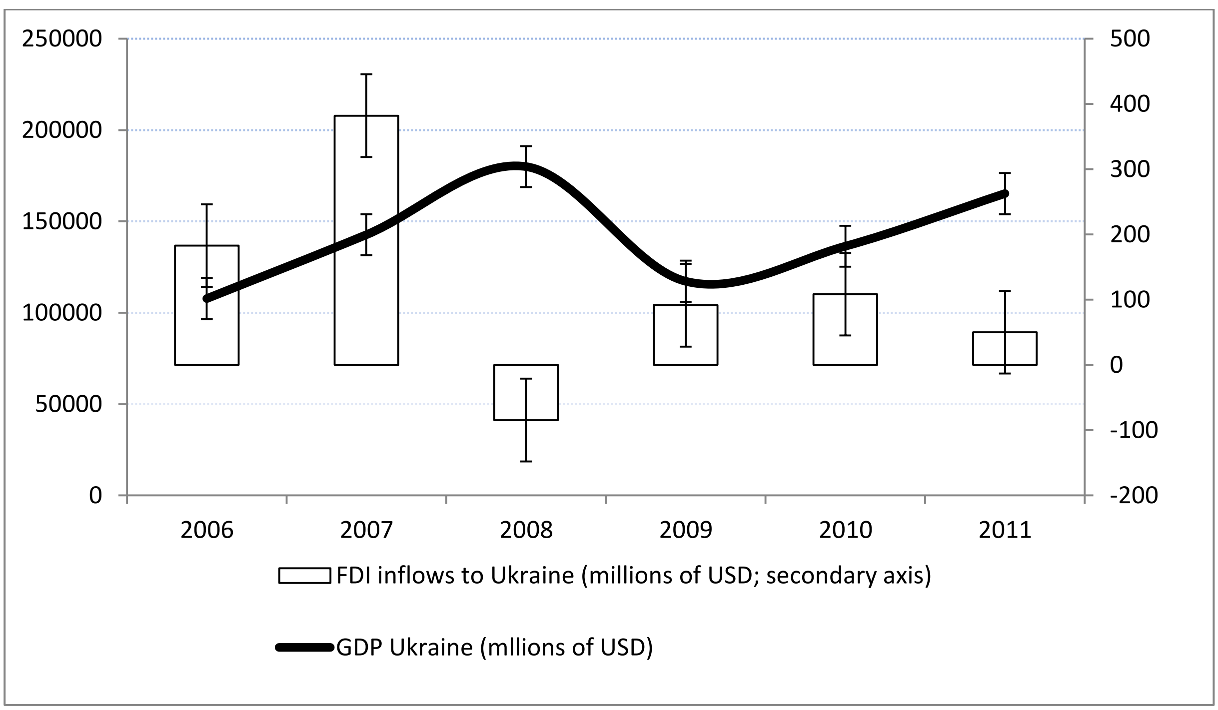
During the first decade of a 21 century less than a half of the Polish FDI choose to entry to foreign markets via Greenfield (48.2%). Varieties of portfolio investments represented (34.5%) of Polish capital flows, and M&A (17.3%). More than half of Polish FDI (51.6%) are subsidiary, joint ventures constituted for 16.8% of total and investments in affiliated companies for 31.5% of outgoing foreign investment. Polish enterprises have been mainly focused on trade (43.7%) and services (36.6%), production and trade (11.5%), production per se (4.3%) and other investment activities 4.0%.

Previous studies of Polish FDI identified differences in the investment perception regarding 'old union', 'the new 12' and the rest of Central and Eastern Europe. The studies showed that investors separate cases for both group of countries that differ when it comes to incentives. In any case however investment decisions have been mainly stimulated by a perspective of finding niche and geographical proximity of existing markets. In terms of location for new investments, Polish entrepreneurs paid attention to the stability of the tax system and legislation (Jaworek, 2012). It is therefore very surprising that so many of them choose Ukraine for the location for a Greenfield investment. It also shows the strength of location incentives in comparison to institutional instability.

The total outflow of capital during investigated period reached 16.1 bln USD. The pick occurred in 2010 (7.2 bln USD). Two years later outflow of FDI from Poland decreased to (0.7 bln USD). Only during the recessive period Polish FDI to Ukraine reached in total 193.5 mln USD. At the end of 2012 most of the financial assets have been located in Luxembourg (5.4 mld USD). A fair amount of investment have been also present in UK (3.1 mld USD), Cyprus (3.1 mld USD) and USA (1.5 mld USD). Over longer period of time, we have also observed that some of the inflows might have a tendency to shift from country to country, depending on the favours of a tax law (example: the case of Great Britain in 2011-2012, respectively 41.1 mil USD and then 162.3 mil USD withdraw year later). When global markets started the adjusting period in 2012 Polish FDI seek opportunities in Netherlands (737.9 mln USD), USA (284.9 mln USD), Hungary (256.9 mln USD) as well as Norway and Russia (respectively 207.0 mln and 191.7 mln USD). During that time investments to Cyprus reached 381.5 mln USD.

Service sector dominates. 70.4% of the total value of Polish FDI flows in to service sectors. Most of the FDI to Ukraine are export related – wholesale, retail and repair of motor vehicles or related services. The rest of the businesses are administrative and supportive.

Figure 5 Polish FDI in Ukraine and GDP Ukraine in 2006-2011.



Source: data.worldbank.org, ukrstat.org.

Investments from Ukraine.

Most FDI from Ukraine came from Donetsk 5.4 bln USD (83.71%), next Dnipropetrovsk 191.2 mln USD (2.95%), Odessa 53.9 mln USD (0.83%), Zaporojian 41.6 mln USD (0.64%) and Lviv 27.4 mln USD (0.42%) (please see the table in the anex). The cumulative value of FDI from Ukraine (UA) reached at the end of 2012, 6.5 bln USD. Most of it, 93% of the total, was invested in the EU. In the 90s, Firms from UA have invested mainly in Russia. After 2006, however they changed their destination almost entirely. Cyprus, become a very popular place to invest. Mainly in sectors like real estate, business supporting services and financial activities (6.83%). In 2012 investments in Russia did not exceed 4.5% of total investments from UA (292.5 mln USD). Six years earlier Russia attracted 42.8% of capital from UA. In the past the most popular destination of UA's investments was trade and repair services (80.44%), and industry (16.42%).

Latvia and Poland are among second popular destinations of Ukraine's FDI. At the end of 2012, the cumulative value of investments from UA to Latvia, added up to 95.5 mln USD (1.5% of the total). Similarly like in Cyprus case these are financial sector investments. The total value of the capital invested in Poland, summed up to 54.2 mln USD (please see the table). According to The State Statistics Committee of Ukraine, the cumulative value of Ukrainian investments in Poland in the end of 2012 reached 54.2 mln (0.8% of total direct investment abroad of Ukraine). This value differs from the estimates of the National Bank Poland (NBP). By the NBP at the end of 2012, Poland attracted 237.3 mln USD of investments from UA.

From 2005, Poland and Ukraine share a number of joint financial and industrial projects. The process have been stimulated by the accelerated privatization in Poland. The examples of cooperation include companies like: The Car Factory in Warsaw (the investor – „Авто-ЗАЗ"), The Metallurgical Plant „Huta Częstochowa" (the inwestor- „ІндустріальнийсоюзДонбасу"), „Gdańsk Shipyard" (the investor – "ІндустріальнийсоюзДонбасу"), the metallurgical industry "Centrostal Bydgoszcz" (the investor – "УкраїнськаГірничо-металургійнаКомпанія").

Development of financial projects fast-tracked a little later and in 2008 companies from UA have been first listed on the Warsaw Stock Exchange. In 2012 on WIG-Ukraine listed there are: „Astarta", „Kernel", „Agroton", „KSG Agro" and „Milkiland", „IndustrialMilk Company", „Ovostar Union", „SadovayaGroup", „CoalEnergy", „Westa ISIC", „KMD Shipping", last but not the least „Agroliga" listed also in New Connect.

Previous attempts to improve investment in Ukraine

Investment climate in UA is subjected to significant inequalities regarding distribution of foreign capital in regional perspective and a low efficiency of inward investment. This could affect spillover effects of the investments, especially if political instability is present. At present this had been reflected by 'a lack of economic and social effects of the presence of foreign capital in the economy of the country'. UA suffers from insufficient amount of credit institutions – also the market is not transparent and risky.

To stimulate the investment government issued a package of investment reports. The structural reform was separated to 5 main blocks (State Agency for Investment and National Project of Ukraine, 2014):

1. InvestPROPOSAL – aimed to create mechanisms that would produce the opportunity to participate in the international investment market projects.

2. InvestINFRASTUCTURE – aimed to create a system of institutions that facilitate the work of foreign investors in Ukraine (inter alia: Ukrainian Development Bank, Regional Development Fund, the Documentation Project Financing Fund and Stateguarantees).

3. InvestPARTNERSHIP – joint international investment projects.

4. InvestMARKETIN –information and marketing campaign, with a positive impact on the investment attractiveness of Ukraine in the world.

5. InvestCLIMATE – made to develop sustainable legislative framework. The majority of bills have been issued by the President of Ukraine; this included: Law of Ukraine "On Industrial Parks," Law of Ukraine "On National Projects", Law of Ukraine "On investment activity" (change), Law of Ukraine "On State Guarantees Administration", Law of Ukraine "On Application of Accounting Statements International Standards".

The Act from January 1st, 2013, "On stimulation of investment activity in sectors of priority in order to create jobs," have been trying to use tax incentives for importers. The same was for other investment projects carried out for priority sectors of the economy. Eligible investments could expect a release from the payment of income tax until 2017 or a release from payment of import duty.[1]

Six months later – in June 1st 2012 new Customs Code came into force, and according to Article 251 of the code, registration of imported goods, that are accounted for a share capital of the company are eligible for a faster customs control. According to the second part of Article 287 of the same code, goods imported for the purpose of further investment (for no less than 3 years) are eligible for release of custom duties.[2]

Early conclusions

Despite the existence of institutions designed to improve the climate of investment and despite initiated reforms, it is still hard for UA to attract FDI and to benefit from spillover

[1]Закон України «Про стимулювання інвестиційної діяльності у пріоритетних галузях економіки з метою створення нових робочих місць» від 06.09.2012 р. № 5205 [Електронний ресурс]. – Режим доступу: http://zakon4.rada.gov.ua/

[2]Концепція державної цільової економічної програми розвитку інвестиційної діяльності на 2011-2015 роки [Електронний ресурс] – Режим доступу: http://zakon2.rada.gov.ua/

effects. The main list of causes for that fact could be formulated as follows:[3] High level of corruption and bureaucracy at various levels of government. There is no transparency in the initial investment process. Significant tax burden. There is a large number of taxes and they sum up to a heavy burden. Yet, previous investigations encountered problems with meeting deadlines for VAT refunds. Difficult and time-consuming registration, licensing and customs procedures; Weak protection of property rights, ownership of land, difficult requirements for starting and running a business. No state protection or guarantee of help for investments; Political instability, no reliable protection against changes in the Ukrainian legislation on foreign investment. Low level of development of market infrastructure and secure cooperation between Ukraine and foreign capital markets.

Further empirical study is needed, however current political situation in Ukraine does not promises reliable results. Foreign investment relations and trade between Poland and Ukraine is determined by national and international laws and agreements. At present, in trade both countries use a Partnership and Cooperation Agreement between the European Communities and their Member States, and Ukraine from 1994 (entered into force in 1998). Ukraine have become a member of WTO in 2008 and Poland in 1967.

Since independence in 1991 Ukraine underwent a series of institutional reforms. It is however difficult to assess whether these reforms have positively contributed to the reduction of investment risks and the costs of doing business. In addition, the uncertainty associated with political destabilization in the region might have a negative impact on investment inflows, portfolio and direct investments in the future.

Ukraine has a good location advantages, large and receptive market, proximity to European markets, rich resource, relatively low competitiveness and market niches. The country has a history of knowledge-intensive activities that have not been successfully privatized.

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Annex

The accumulated value of foreign investments in Ukraine in mln USD, in the form of FDI in 2007-2012.

	2007	2008	2009	2010	2011	2012
The updated value of FDI inflow to Ukraine	29542,7	35616,4	40053	44806	50333,9	54462,4

* as of January 1st next year, calculated as the updated value since the start of the investment.
Source : The State Statistics Committee of Ukraine, 2012

The geographical structure of foreign capital in the form of FDI in Ukraine in 2012 mln USD.

Countries	The value of FDI	% of share
Overall this:	54462,4	100,0
Cyprus	17275,1	31,7
Germany	6317,0	11,6
The Netherlands	5168,6	9,5
Russia	3785,8	7,0
Austria	3401,4	6,2
Great Britain	2556,5	4,7
Virgin Islands	1884,9	3,5
France	1765,3	3,2
Sweden	1600,1	2,9
Switzerland	1106,2	2,0
Italy	1015,9	1,9
USA	936,7	1,7
Poland	916,4	1,7
other countries	6732,5	12,4

* as of January 1st next year, calculated as the updated value since the start of the investment.
Source : The State Statistics Committee of Ukraine, 2012

Foreign direct investment in the regions of Ukraine in mln USD, in 2007 and 2012

Districts	2007		2012	
	The value	% of share	The value	% of share
Ukraine	29542.70	100	54462.40	100
AR of Crimea	726.2	2.46%	1463.7	2.69%
Vinnicki	152.6	0.52%	245.4	0.45%
Volyn	392.4	1.33%	361.2	0.66%
Dnipropetrovsk	2934.3	9.93%	8351.8	15.33%
Donetsk	1355.2	4.59%	2981.6	5.47%
Zhytomyr	173.6	0.59%	363.8	0.67%
Transcarpathian	345.3	1.17%	407.2	0.75%
Zaporizhia	761.4	2.58%	1144.2	2.10%
Ivano-Frankivsk	385.2	1.30%	642.5	1.18%
Kiev	1083.6	3.67%	1927.7	3.54%
Kirowogradski	55.3	0.19%	103.7	0.19%
Luhansk	309.1	1.05%	838.5	1.54%
Lviv	771.5	2.61%	1634.8	3.00%
Mikolajevski	136.8	0.46%	259.9	0.48%
Odessan	880.8	2.98%	1629.5	2.99%
Poltava	367.9	1.25%	942.8	1.73%
Rovenskaya	233.1	0.79%	296.9	0.55%
Sumy	180.5	0.61%	374.4	0.69%
Ternopil	51.0	0.17%	64.6	0.12%
Kharkiv	1278.7	4.33%	2170.4	3.99%
Kherson	156.2	0.53%	245.2	0.45%
Khmelnitsky	129.0	0.44%	208.6	0.38%
Czerkaski	175.0	0.59%	884.1	1.62%
Chernivtsi	51.2	0.17%	64.3	0.12%
Czernihovski	86.6	0.29%	105.3	0.19%
Kyiv	9681.7	32.77%	26592.1	48.83%
Sevastopol	147.2	0.50%	158.4	0.29%

** as of January 1st next year, calculated as the updated value since the start of the investment.

Source : The State Statistics Committee of Ukraine, 2007 and 2012.

Industry structure of foreign capital in the form of FDI in Ukraine in mln USD, in 2007 and 2012

Specification	2007		2012	
	The value	% of share	The value	% of share
In general:	29542,7	100	54462,4	100%
financing activities	4869,1	16,5%	16105,6	29,6%
industry in general that includes:	8004,1	27,1%	17166,7	31,5%
processing industry such as :	6813,0	23,1%	14078,7	25,9%
mineral industry	704,2	2,4%	1053,9	1,9%
manufacture of food products	1561,2	5,3%	3039,9	5,6%
metallurgical industry and manufacture of fabricated metal products	1596,7	5,4%	6157	11,3%
chemical and petrochemical industry	840,8	2,8%	1325,8	2,4%
other branches of the processing industry	2110,1	7,1%	2502,1	4,6%
extractive industry	1052,7	3,6%	1548,4	2,8%
production and supply of electricity, gas and water	138,4	0,5%	1539,7	2,8%
Real estate, business services	2669,3	9,0%	9058,5	16,6%
architecture	1631,8	5,5%	974,1	1,8%
Trade, repair services	3072,1	10,4%	6003	11,0%
Transport and communication	1274,4	4,3%	3015,7	5,5%
Agriculture and forestry	557,3	1,9%	800,7	1,5%
Other business activities	7464,6	25%	1338,1	2%

*as of January 1st next year, calculated as the updated value since the start of the investment.
Source : The State Statistics Committee of Ukraine, 2007 and 2012.

Geographical structure of Ukrainian FDI abroad in mln USD in 2012.

Country / sector of the economy		2012	
		The value	% of share
In total		6481.9	100
EU countries		6046	93.28%
1	Cyprus	5810.5	89.64%
	Real estate, business services	5331.8	91.76%
	financing activities	422.7	7.27%
2	Latvia	95.5	1.47%
3	Poland	54.2	0.84%
	Trade, repair services	43.6	80.44%
	industry	8.9	16.42%
4	Other EU countries	85.8	1.32%
The CIS countries		340.6	5.25%
5	Russia	292.5	4.51%
	industry	113.8	38.91%
	Trade, repair services	80.4	27.49%
6	Kazakhstan	25	0.39%
	Trade, repair services	24.9	99.60%
7	Other CIS countries	23.1	0.36%
The other countries		132	2.04%

* as of January 1st next year, calculated as the updated value since the start of the investment.
Source : The State Statistics Committee of Ukraine, 2012

Foreign direct investment in the regions of Ukraine that are abroad in 2007 and 2012 (in mln USD)

Districts	2007		2012	
	The value	% of share	The value	% of share
Ukraine	6196.6	100	6481.9	100
AR of Crimea	0.2	0.00%	2.2	0.03%
Vinnicki	0.2	0.00%	0.2	0.00%
Volyn	…1		…1	
Dnipropetrovsk	88.7	1.43%	191.2	2.95%
Donetsk	5335.1	86.10%	5426.3	83.71%
Zhytomyr	-		-	
Transcarpathian	-		…1	
Zaporizhia	8.7	0.14%	41.6	0.64%
Ivano-Frankivsk	…1		…1	
Kiev	2.5	0.04%	7	0.11%
Kirovogradski	…1		0.1	0.00%
Luhansk	1.7	0.03%	11.1	0.17%
Lviv	0.9	0.01%	27.4	0.42%
Mikolajevski	0.5	0.01%	0.8	0.01%
Odessa	35.7	0.58%	53.9	0.83%
Poltava	2.3	0.04%	2.3	0.04%
Rovenskaya	-		-	
Sumy	3.4	0.05%	2.7	0.04%
Ternopil	…1		…1	
Kharkiv	63.9	1.03%	12.9	0.20%
Kherson	0	0.00%	0.1	0.00%
Khmelnitsky	…1		…1	
Czerkaski	…1		-	
Chernivtsi	…1		…1	
Czernihowski	…1		-	
Kyiv	629	10.15%	671.1	10.35%
Sevastopol	…1		…1	

*as of January 1st next year, calculated as the updated value since the start of the investment.
Source : The State Statistics Committee of Ukraine, 2012