SigmaBleyzer

Where Opportunities Emerge.

Attracting Investments To Ukraine

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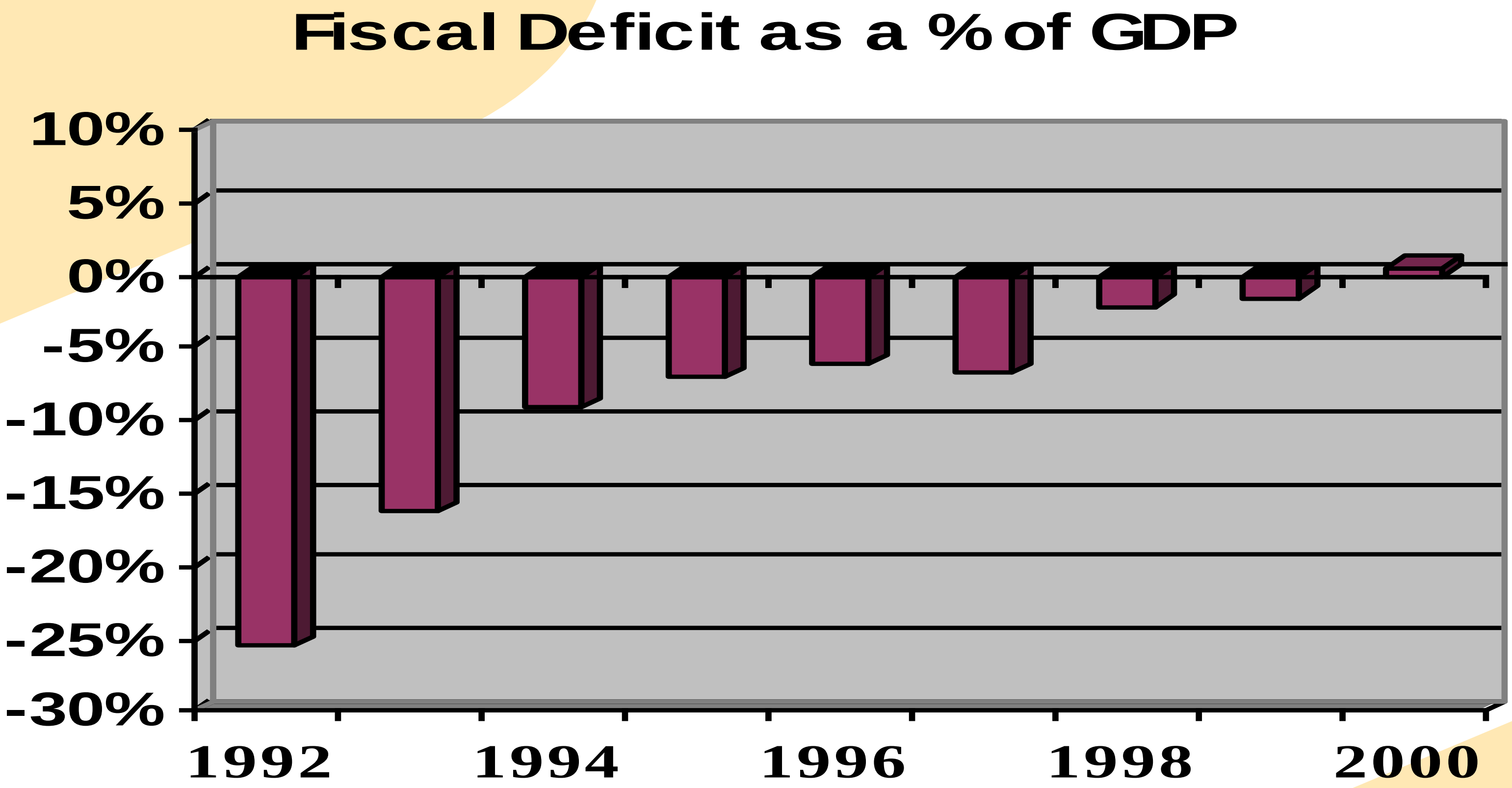
Ukraine 2000

- Major turning point
  - First GDP Growth since independence - 6%
  - High Industrial Output Growth - 12.9%
  - High Agricultural Output Growth - 9.2%
  - Real Income Growth of 8.5%
  - Population deposits in commercial banks up 45%
  - Positive foreign trade and current account balance
  - Stable foreign exchange rate
  - International reserves up 80%
  - External public debt down 17%
- Two years ago, these results would have been just a dream...

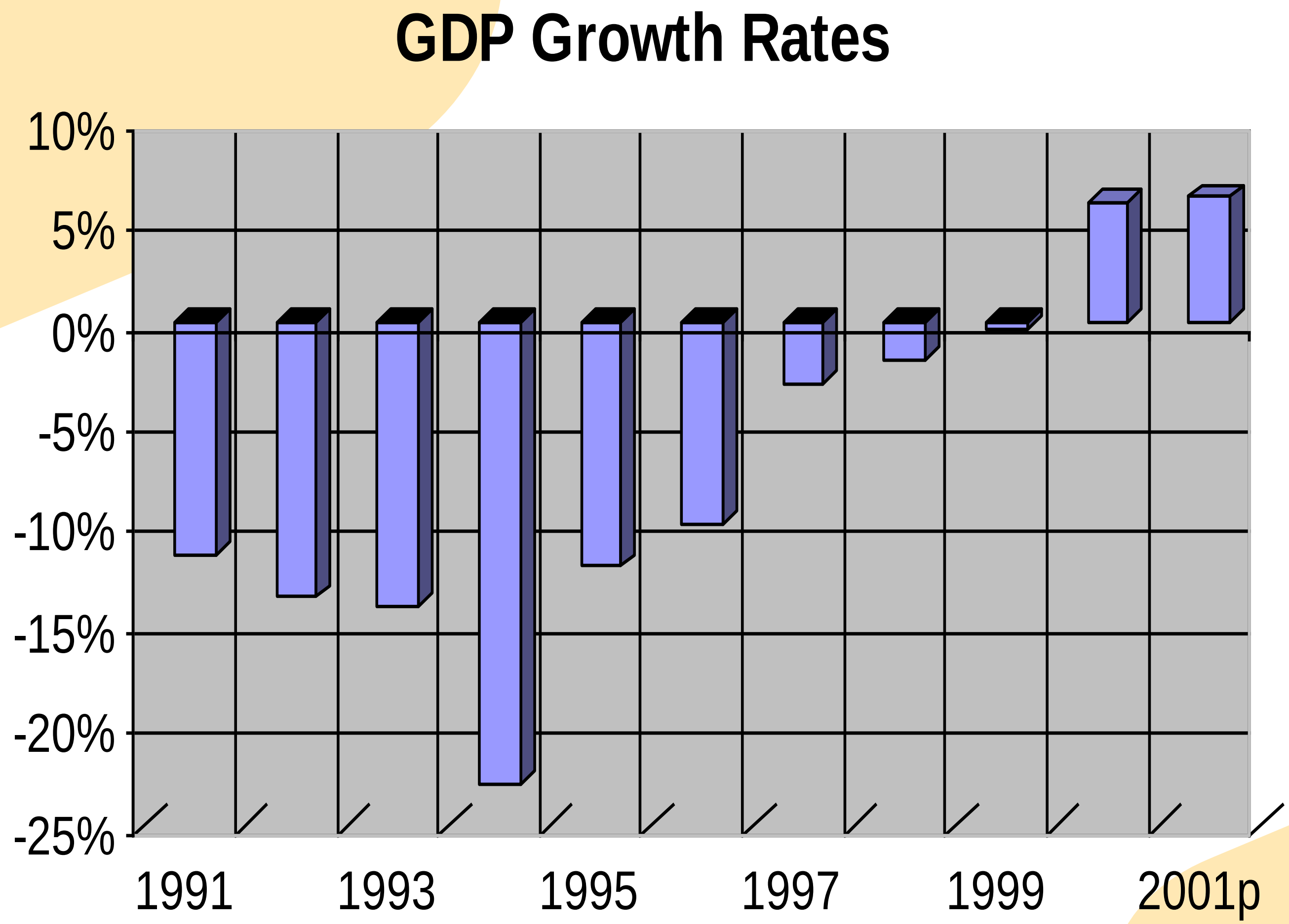
What Happened?



Any other Factors?

- Land reform, land certificates, titles proceeding. Land Code now approved
- Elimination of Government interference in Agriculture
- Barter – down dramatically, cash collections in the energy sector up from 12% in 1999 to 85% of sales
- Significant reduction of barter in international trade
- Elimination of Government pension arrears
- Major reduction in Government wage arrears
- Introduction of European import certification standards
- Customs procedures improvement closer to European standards

Critical Mass of Reforms?



2001 – Is Growth Sustainable?

- January – October: real GDP up by 9.1% , industrial output up by 16. 1%.
- Inflation – 3.9% in the first 10 months of 2001
- Fiscal policies produced surplus in the first 8 months of 2001 (including privatization revenues) of UAH 1.5 billion or 0.7% of GDP
- In 2001, international reserves went up 95% to $3.1 billion, the highest level since independence.
- Foreign debt down another 6% to $9.7 billion.
- The domestic currency has been stable.
- IMF and World Bank renewed lending operations on September 20 ($376M+$250M).

- The **extraordinary** economic performance of Ukraine in the last 22 months presents a unique opportunity for a breakthrough
- **But Domestic Investments are still low and foreign investment continues to decline**
- Major increase in the investment flows is necessary to sustain long-term growth

1. What is what international investors want?

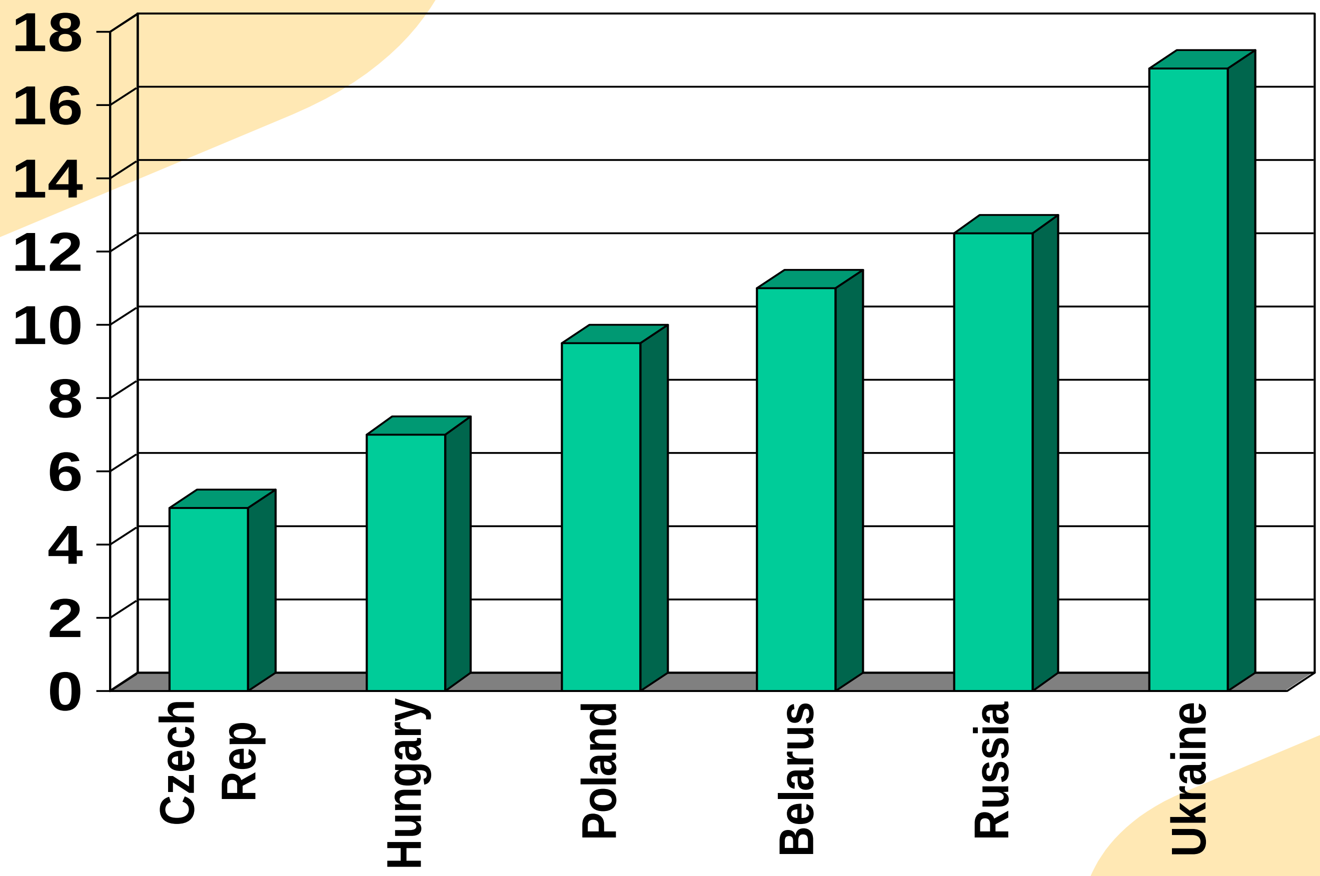
- Transparency:
  1. All necessary business information should be open.
  2. The basis for business decisions should be understood.
  3. Financial statements should reflect the real situation of the enterprises.
- Simplicity
  1. Business procedures (such as licenses, registration, etc) should be uncomplicated, easy to understand and easy to implement.
  2. Business processes, such as capital transfers, should be easy to execute.
- Predictability
  1. The "rules of the game" should be clear and stable
  2. Laws should ensure a level playing field, making obligations and property rights more predictable .

- What is what international investors receive?

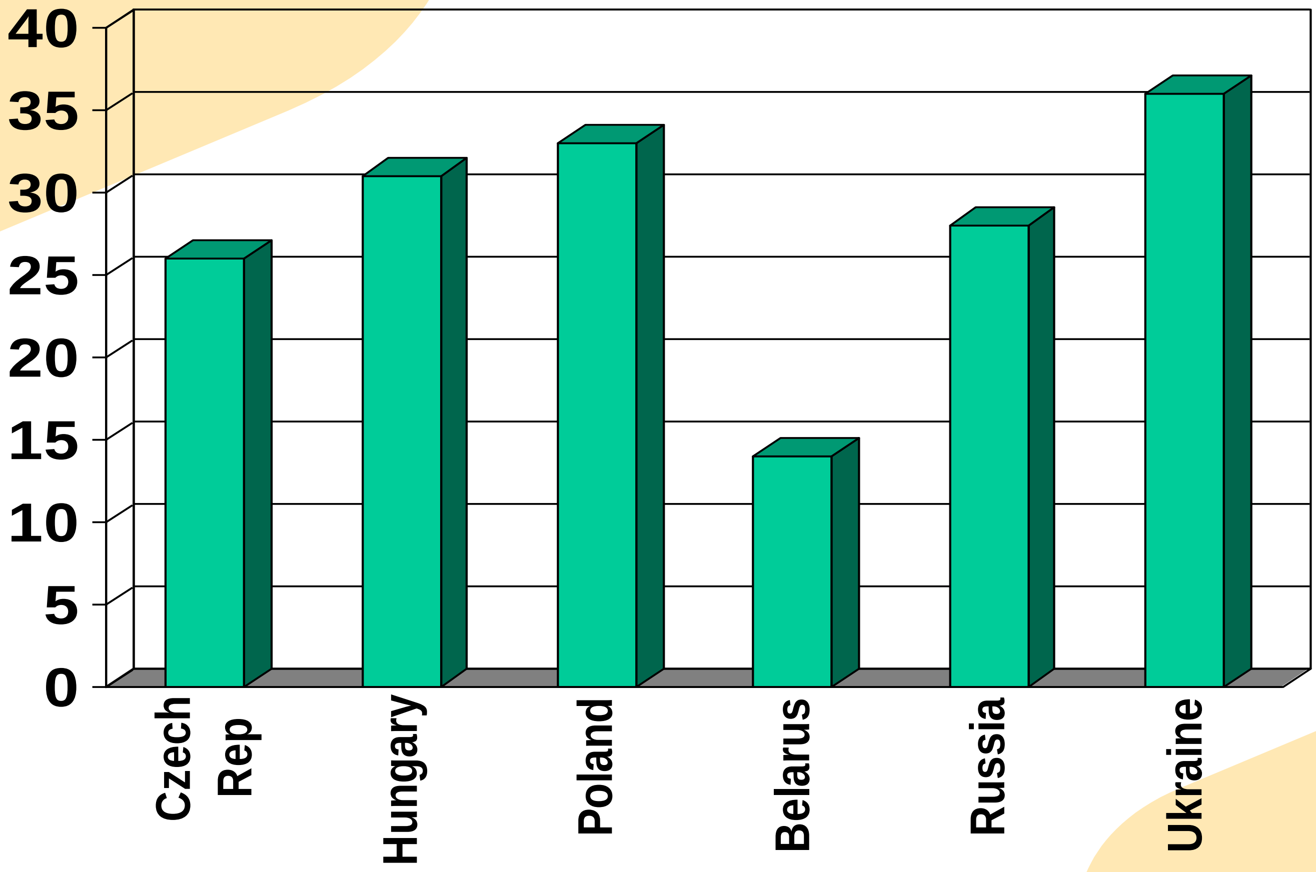
A business survey by the ICPS shows that 65 major foreign companies in Ukraine are worried with:

  - The instability and exorbitance of Gvt. regulations
  - Ambiguities of the legal system
  - Uncertainty of the economic environment
  - Corruption
  - High Tax burden
  - Problems establishing clear ownership rights
  - Difficulty negotiating with Government authorities
  - Volatility of the political environment
    - What is the evidence of these claims?

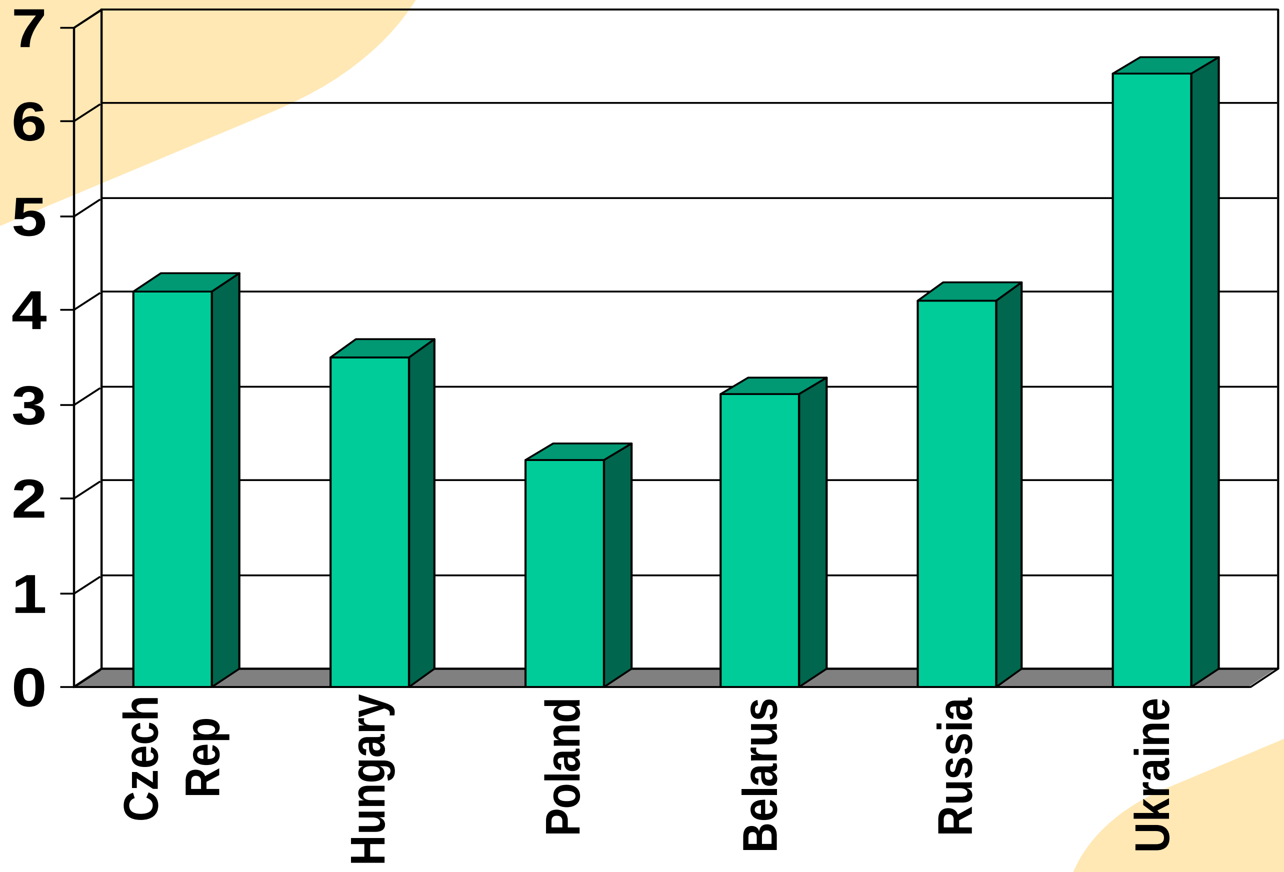
- Percentage of Management Time Spent on Regulatory Issues:



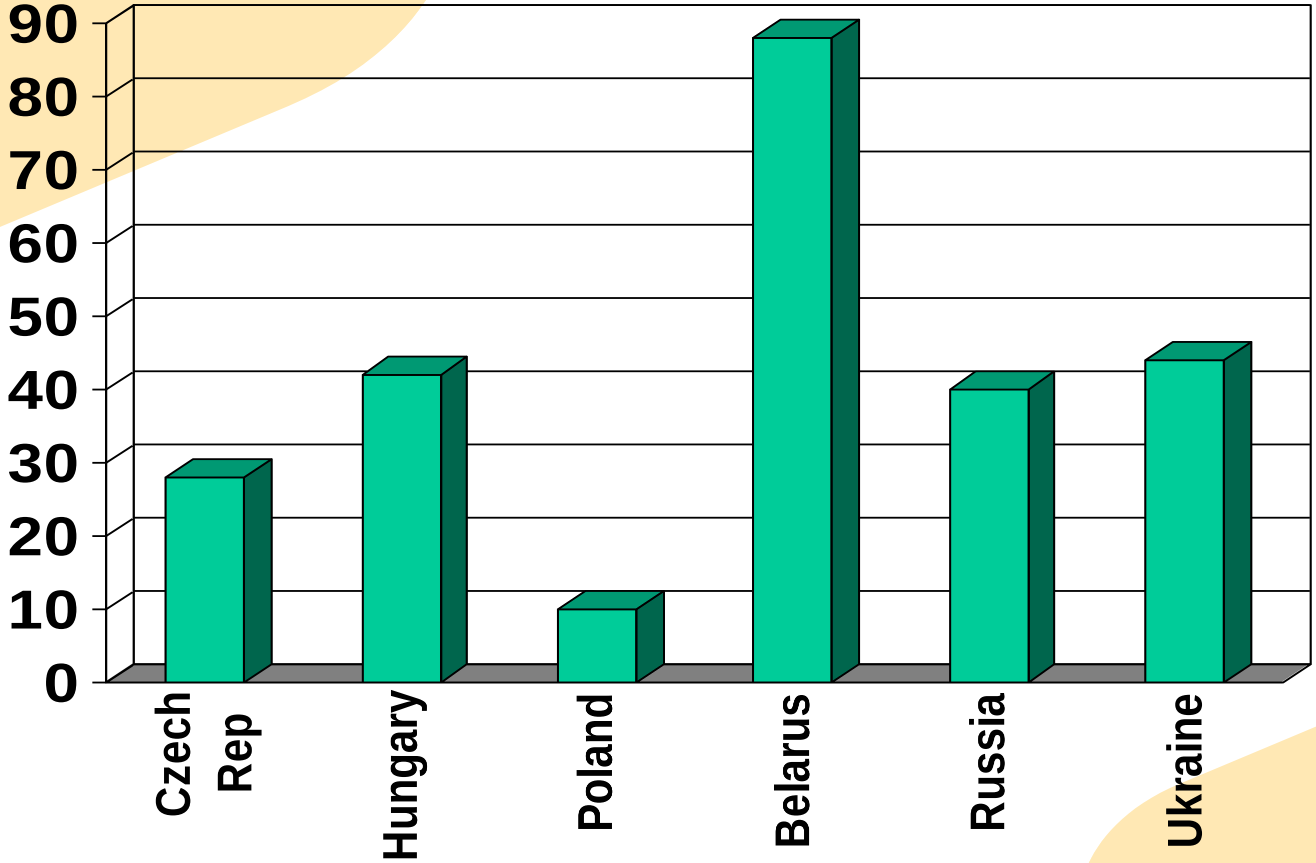
- Percentage of Firms Bribing “Frequently” or More:



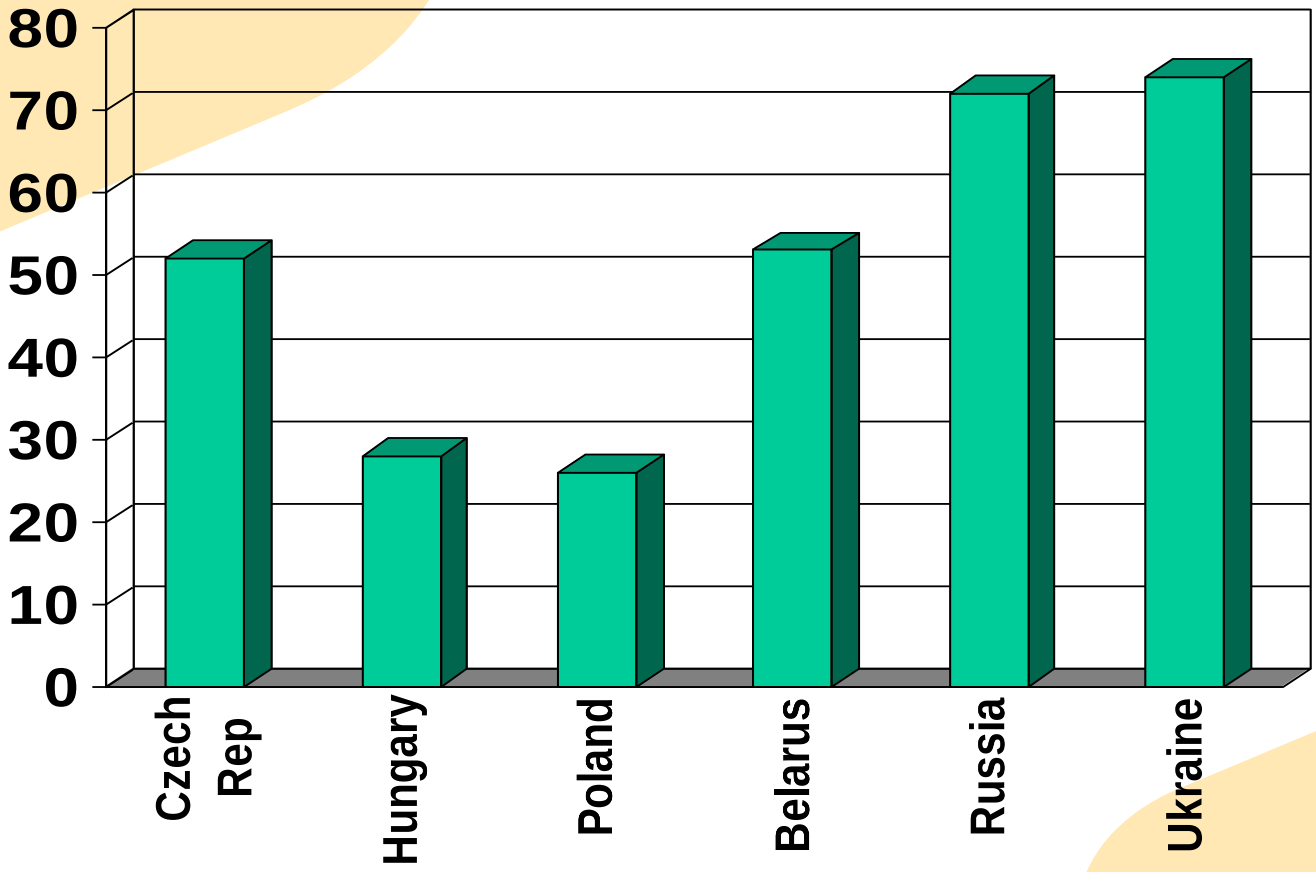
- Cost of Bribes as a Percentage of Revenues:



- Percentage of Firms Reporting State Interventions in Enterprise Pricing Decisions:



- Percentage of firms insecure in their property and contract rights:



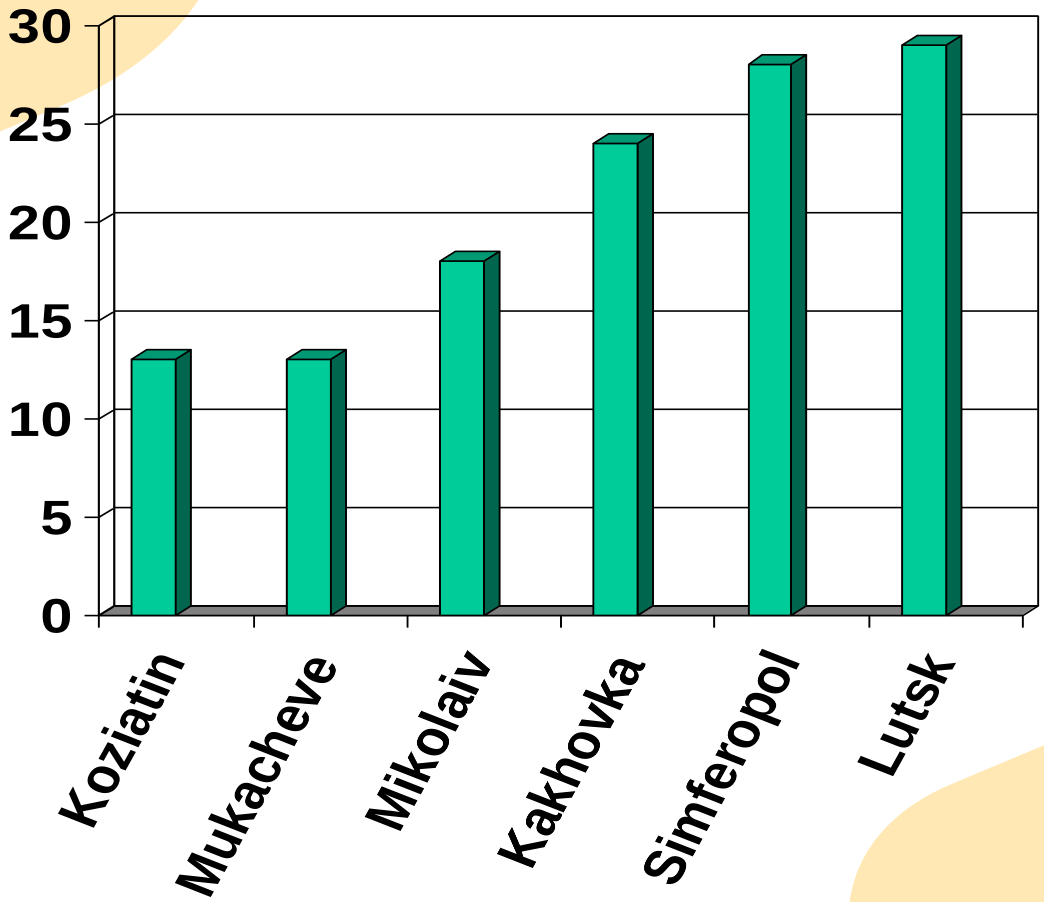
1. What can a Local Government do?

The good news is that there are major variations in all these variables that affect the business climate across Oblast and Cities in Ukraine.

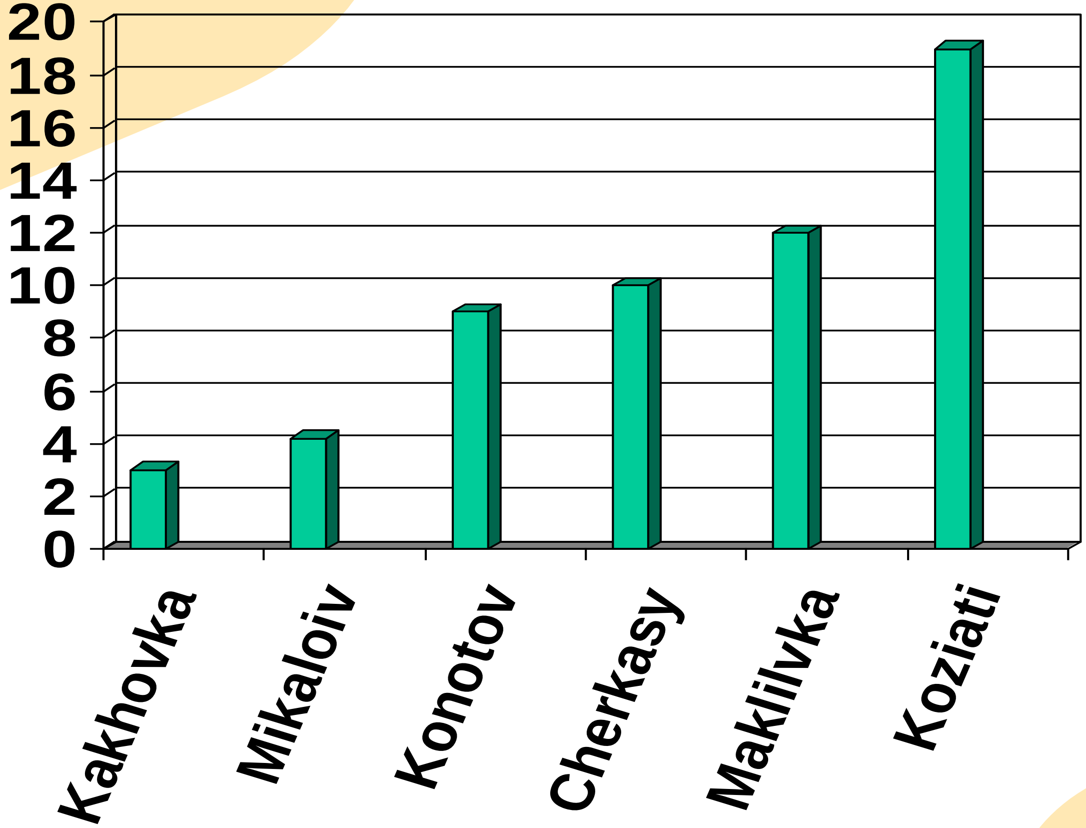
This means that local administrations may have a lot to say on creating a favorable business environment

A few examples follows:

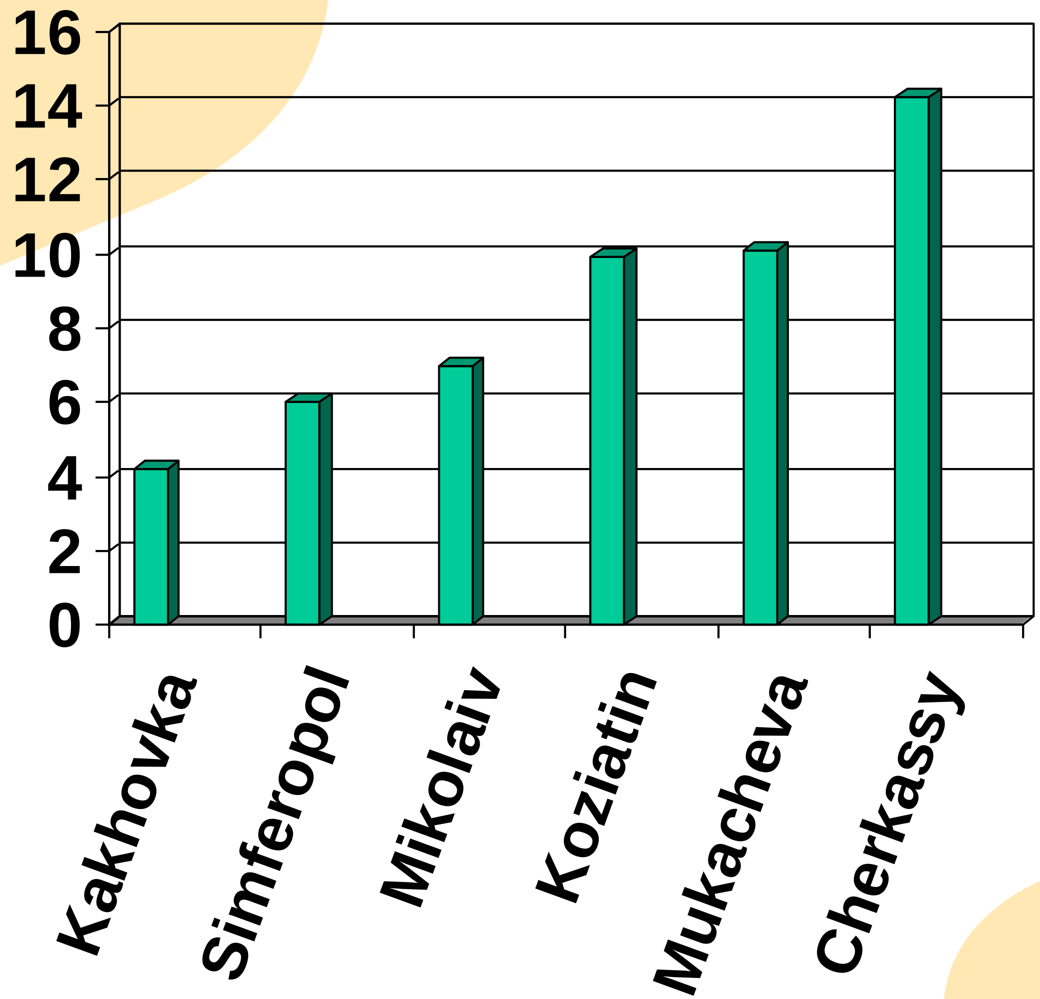
Average Time to Obtain a License (days)



Unofficial Types of Permits/Permissions



Average Number of Inspections per enterprise per year



Creation of the International Private Capital Task Force (IPCTF) for Ukraine

- Given this evidence, can we systematically identify the Government policies that may have the greatest impact on investments:
- IPCTF effort objective: Statistical analysis and benchmarking of other economies to identify and quantify best practices in government policies, which improve investment climate and attract private capital

IPCTF Steering Committee

Private Companies:* *AGCO, SigmaBleyzer, Coca Cola, Citibank, Commerzbank, Credit Lyonnais, FMI, PricewaterhouseCoopers, Leo Burnett, DuPont.

Agencies: EBRD, IMF, IFC, USAID, European Commission, World Bank, US Embassy, American Chamber of Commerce, International Center for Strategic Studies, Harvard Institute for International Development.

Countries Included in Statistical Analysis

Angola, Argentina, Armenia, Azerbaijan, Belarus, Bolivia, Botswana, Bulgaria, Burkina Faso, Cameroon, Chile, Colombia, Costa Rica, Croatia, the Czech Republic, Ecuador, Egypt, El Salvador, Estonia, Ethiopia, Ghana, Hungary, India, Indonesia, Jordan, Kazakhstan, Kenya, Lithuania, Malawi, Moldova, Morocco, Mozambique, Nigeria, Peru, Philippines, Poland, Romania, Russia, Senegal, Slovak Republic, South Africa, Tanzania, Tunisia, Turkey, Uganda, Ukraine, Venezuela, Vietnam, Zambia, and Zimbabwe.

Key Drivers / Policy Action Groups

- ***The study pre-condition is macroeconomic stabilization, resulting from sound fiscal and monetary policies.***
- Study identified the following key government policy actions, which stimulated foreign direct investments in successful transition economies:

  1. **Liberalize and De-Regulate Business Activities**
  2. **Provide a Stable and Predictable Legal Environment**
  3. **Enhance Governance & Reform Public Administration**
  4. **Remove International Capital & Trade Restrictions**
  5. **Facilitate Financing of Businesses**
  6. **Eliminate Corruption**
  7. **Reduce Political Risks (non-economic country risks)**
  8. **Expand Country Promotion**
  9. **Rationalize Investment Incentives**

- The study found that about 60% of the variations in the flows of Foreign Direct Investments in the group of 50 countries could be explained by the above policy actions, particularly the first three.

Benchmarking Results

UKRAINE	RUSSIA	POLAND	HUNGARY	CHILE	ARGENTINA

Business Liberalization Score

18	49	87	80	89	62

Legal Environment Score

17	62	99	93	89	65

Financial Sector Score

10	39	62	68	74	39

Governance and Privatization Score

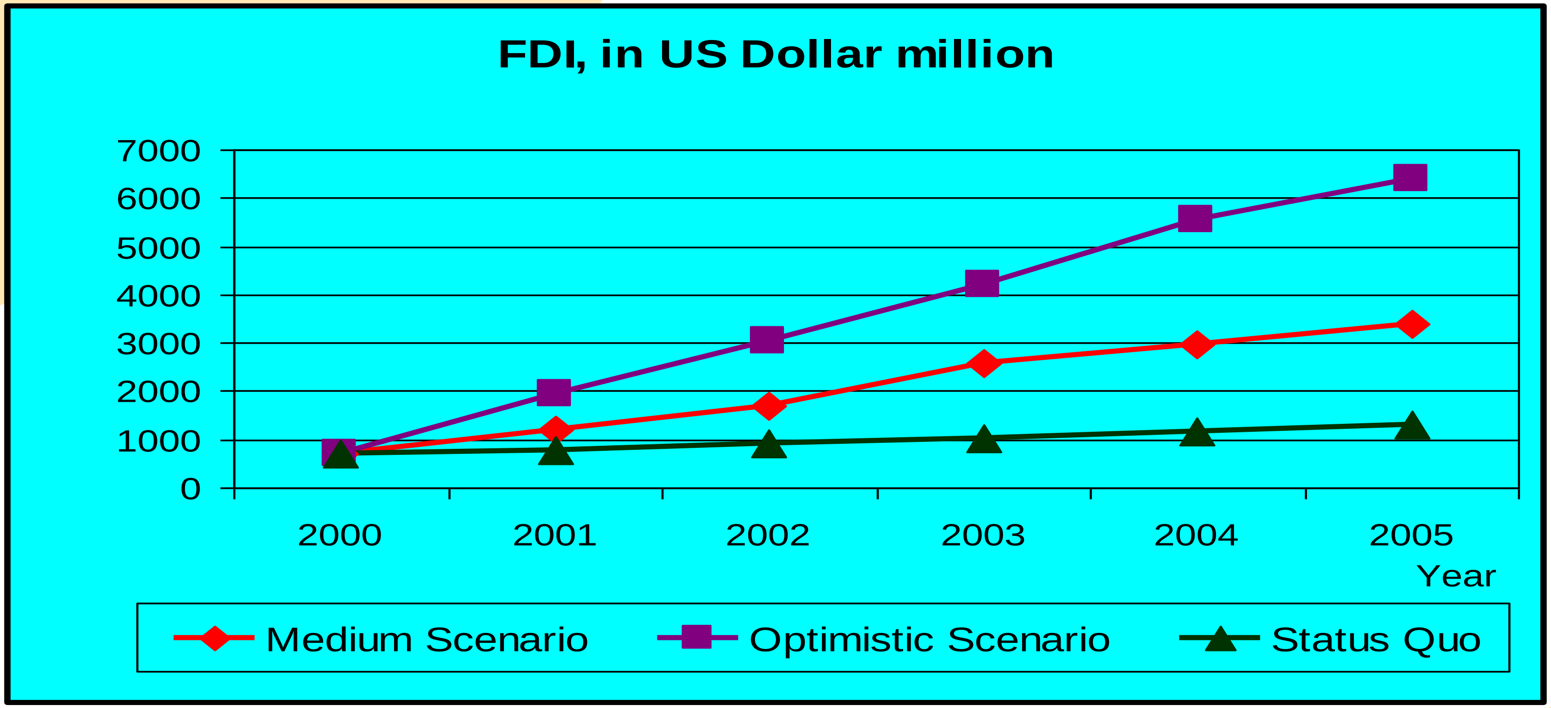
29	30	89	82	80	65

Benchmarking Results

UKRAINE	RUSSIA	POLAND	HUNGARY	CHILE	ARGENTINA
Political Risk Score					
65	49	83	82	71	75
International Capital Controls & Foreign Trade Score					
63	45	78	79	84	69
Corruption Score					
15	21	41	52	74	35
Governmental Promotional Effort Score					
20	30	80	100	90	75
Tax and Investment Incentives Score					
31	48	78	82	63	70

FDI For Ukraine- Possible Scenarios

- Ukraine's government policies will determine the FDI flows over the next 15 years (5 years shown)



- The Middle Scenario would generate an incremental GDP growth rate of 4.8% per annum.

Conclusions for Ukraine

- **With continuation of current policies**, FDI flows **will not increase** from its current level of under **US$1.0 billion per year** (except for ad-hoc flows related to large privatizations)
- **Under a middle scenario**, with policy actions to **reduce in five years 50%** of the policy level differential with the Bests-in-Class, Ukraine could increase FDI to about **US$3.4 billion per year by 2005, resulting in US$75 billion over the next 15 years**
- **Under a more aggressive scenario**, with stronger policy actions to **reduce in five years 80%** of the policy level differential with the Bests-in-Class, the level of foreign direct investments could increase to **US$6.4 billion per year by 2005, resulting in US$100 billion over the next 15 years**

IPCTF Framework – A Tool for Action

- Low correlation between FDI flows and "natural characteristics" (e.g., location, size, resources, etc.)
- High correlation between government policies and FDI flows
- Measuring economic impact of government policies based on the gap between the policies of the country and the policies of the best-in-class in each of the nine government policy areas
- Econometric model of a transition economy can then predict FDI flows based on changes in government policies
- IPCTF Framework provides a **comprehensive tool** for building consensus and developing an **Action Plan** for country and also for any local government.

Ukraine 2001 – A Call for Action

- Ten years in Transition
- Approaching the critical mass of reforms
- Significant economic turnaround in the making
- Need investments to sustain and accelerate economic growth
- IPCTF Action Plan for Ukraine is a comprehensive plan to successfully complete Ukrainian transition to market economy and democracy
- Political Will is needed to enact the Action Plan.
- Central as well as Oblast Governments must act.
- Support of the international community is essential.

BLEYZER INITIATIVE

- Use the IPCTF framework to create a business environment that is capital-friendly.
- Leverage private capital with donor’s money.
- Refocus multilateral and bilateral assistance on creating private businesses – particularly SMEs
- Maximize private equity investments in place of debt, structuring financial assistance as “private equity funds” managed by private money managers.
- Minimize government-to-government money transfers.
- Implement comprehensive coordinated assistance program to the FSU countries: use donor capital to create the environment, which attracts private capital.

A Plan Of Action For Local Governments

- Develop a Program to implement measures to improve the nine investment drivers identified by the IPCTF.
- Define and widely disseminate the role of the local government as that of supporting - and not replacing - private sector activities.
- Reduce the number of separate local government agencies that have the power to interfere/interact with private business.
- Adopt clear and enforceable rules to limit the power of state officials on monitoring and interfering with local business.
- Develop mechanisms to ensure the compliance by local officials with the above and national legislation requirements.
- Introduce more transparency in decision-making at the oblast, rayon and town levels.
- Publish clear and transparent accounts of local finances.
- Develop mechanisms to ensure that entrepreneurs have proper recourse against local officials.
- Raise the salaries of key civil servants to attract quality staff and make them less susceptible to corruption.