Ukraine’s Untapped Investment Potential

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Ukraine Need FDIs to Realize its Potential

- Foreign direct investments (FDIs) are important drivers for sustained productivity and economic growth in emerging market economies.
- However, **Ukraine has consistently underperformed its regional and other peers in attracting FDIs**;
- The gap between Ukraine and other Central European countries in attracting FDI flows was large even when external financing was readily available: this happened because **foreign investors were discriminating against poorly governed economies**.
- Ukraine lagged other developing regions in the world as well.
- With the current high global risk aversion and tight financing, attracting FDI will become even more challenging as Ukraine will have to compete with countries whose investment climate is more business friendly.
FDI per capita in Ukraine vs. European Countries (US$)

Source: World Bank
FDI per capita in Ukraine vs. Other Regions (in US$)

Source: World Bank
Ukraine has some globally competitive factors

**Relative ranking of the five peer economies versus Ukraine**

**Basic drivers of competitiveness**
- better than Ukraine
- worse than Ukraine

**Advanced drivers of competitiveness**
- better than Ukraine
- worse than Ukraine

- **Infrastructure**
- **Health and primary education**
- **Higher education and training**
- **Market size**
- **Institutions**
- **Macroeconomic environment**
- **Technological readiness**
- **Innovation**

- **Chile**
- **South Africa**
- **Georgia**
- **Lithuania**
- **Poland**

- Ukraine has some good basic drivers of competitiveness, such as educated labor force, infrastructure and market size.
- But low quality of institutions, unstable economy and the lack of innovation are big obstacles to the country’s ability to attract FDIs.

Source: Global Competitiveness Report 2014
Yet, doing business is a very risky venture in Ukraine.

Reduce barriers to starting a new business

- Ukraine has made good progress on “Starting a Business”.
- Today it is relatively easy to start a business in Ukraine; yet there is still room to cut the number of steps (currently 6) and time (21 days); for example, by combining registration in the Registration Office and Tax Authority.
- But in Ukraine it still takes nearly a year to obtain access to the electricity grid versus about 2 months in Georgia or just 30 days in Chile.

Simplify business taxation

• Tax compliance is a huge burden on Ukrainian businesses, mostly due to unnecessary complicated taxation of labor income and myriad social payments.
• Paying income tax involves a single payment in Chile and Georgia and can be filed online in Georgia; in Ukraine, there are about 24 annual payments of labor taxes and contributions.
• Simplify labor income taxation and move much of the tax compliance paperwork online.  

Enhance the protection of private property rights

- It is still too costly and time-consuming to register property, enforce contracts and resolve insolvency in Ukraine – all of which deters the creation of more efficient and competitive businesses.
- Investors in Ukraine suffer from a weak rule of law, corrupt judiciary and inefficient redress mechanisms to protect their rights.

Improve public governance

**World Bank Governance Indicators**

percentile rank

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<th>Voice and accountability</th>
<th>Government effectiveness</th>
<th>Regulatory quality</th>
<th>Rule of Law</th>
<th>Corruption</th>
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- The quality of public governance in Ukraine remains consistently below the level of government effectiveness in most emerging economies.
- Government still remains unaccountable, inefficient and inept at creating business-friendly regulatory environment.
- Weak rule of law and endemic corruption is particularly worrisome.
- **There is an urgent need to enact a comprehensive Public Administration Reform, overhaul regulatory and taxation rules, fix the legal and judicial system and reduce corruption.**

Source: World Bank – Governance Indicators
**Investment opportunities: Agriculture**

- Grains production and exports are growing.
- Yet, yields of staple crops remain low.
- **The investment environment in the agro sector must be improved: there is a need to simplify agricultural regulations, streamline licensing procedures for grain exporters; promote investments in modern machinery, seeds and fertilizers; enhance R&D activities, and improve infrastructure.**
- State-owned land should also be made available to private firms.

Source: State Statistics Committee, UN Comtrade, FAO
Investment opportunities: Energy sector

- Energy supply is not diversified – almost all energy imports have been coming from Russia.
- Furthermore, energy use in Ukraine remains extremely inefficient.
- Energy Government policy should:
  1. Encourage the diversification of energy imports. (For example, provide support to LNG projects).
  2. Attract investments into the development of domestic conventional and alternative energy resources.
  3. Improve energy efficiency of the economy.

Source: UN Comtrade, World Bank