IMPORTANCE OF FOREIGN DIRECT INVESTMENTS FOR ECONOMY OF UKRAINE

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Abstract: *Foreign direct investments (FDI) are considered nowadays a significant determinant of economic growth. Many governments of developing as well as developed countries are trying to attract FDI. A lot of countries not only decided to liberalize their markets, governments of many countries also started to offer generous investment packages, such as import duty exemptions, tax holidays or preferential loans, in order to attract inflows of FDI. The research focuses on the analysis of FDI inflows to Ukraine. The research purpose is to study the importance of Ukraine's participation in the international movement of capital, such as FDI to Ukraine.*

Keywords: FDI inflows to Ukraine, Ukrainian economy

Introduction

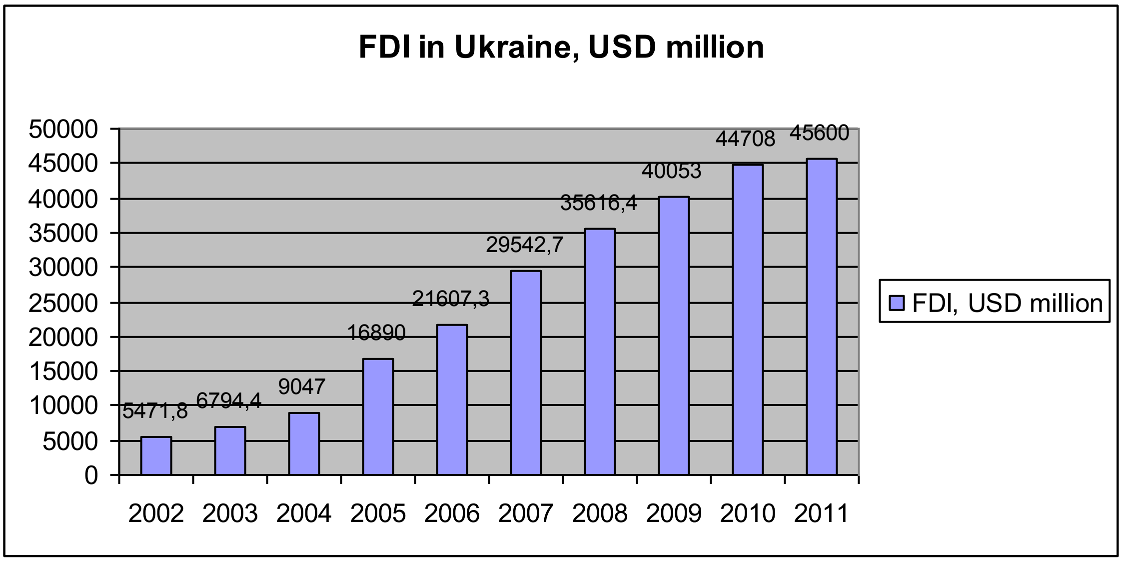
Studies of investment problems in economy have always been the focus of economic science. This is because investments affect the underlying basis of economic activity. In modern terms they are the most important means of ensuring the conditions for exit from the economic crisis, structural shifts in the economy, technical progress, improving the quality indicators of economic activity at the micro and macro levels. Enhancing the investment process is one of the most effective mechanisms for socioeconomic transformation. Furthermore, FDI is a fuel for the developing economies. More firms in more industries from more countries are expanding abroad through direct investment than ever before and virtually all economies now compete to attract multinational enterprises Through out the world countries are interested in attracting FDI into their economies. The investment climate that includes fundamentals and institutions, have a great impact on the FDI flow into the country. Ukraine urgently needs FDI in almost every area from agriculture to telecommunications. The government has publicly stated it seeks foreign investment, but thus far it has failed to create an attractive investment climate, in spite of recent numerous but uncoordinated steps in that direction. Large parts of the country's capital stock have not been maintained or replaced during the last decade, and there has been little new investment. A considerable contribution to development of this problem was done by such scientists economists, as Y.V. Makogon, A.M. Guarantor, A.C. Filipenko. O.I. Rogach. The purpose of the article is determination of role of the foreign investing in the economy of Ukraine.

Research results and discussion

Foreign investments are values which are invested by foreign investors in facilities investment in accordance with the law of Ukraine "On foreign investments" [1]. Foreign investments - an important part of the structure of the investment resources of Ukraine. Joining them on the market the country contributes to growth of production, technological rise of industrial production output in world markets and improves formation of the national market. Accelerating the pace of reform of the Ukrainian economy requires a growing number of investment resources for individual companies, regional development and for Ukraine's economy as a whole [2].

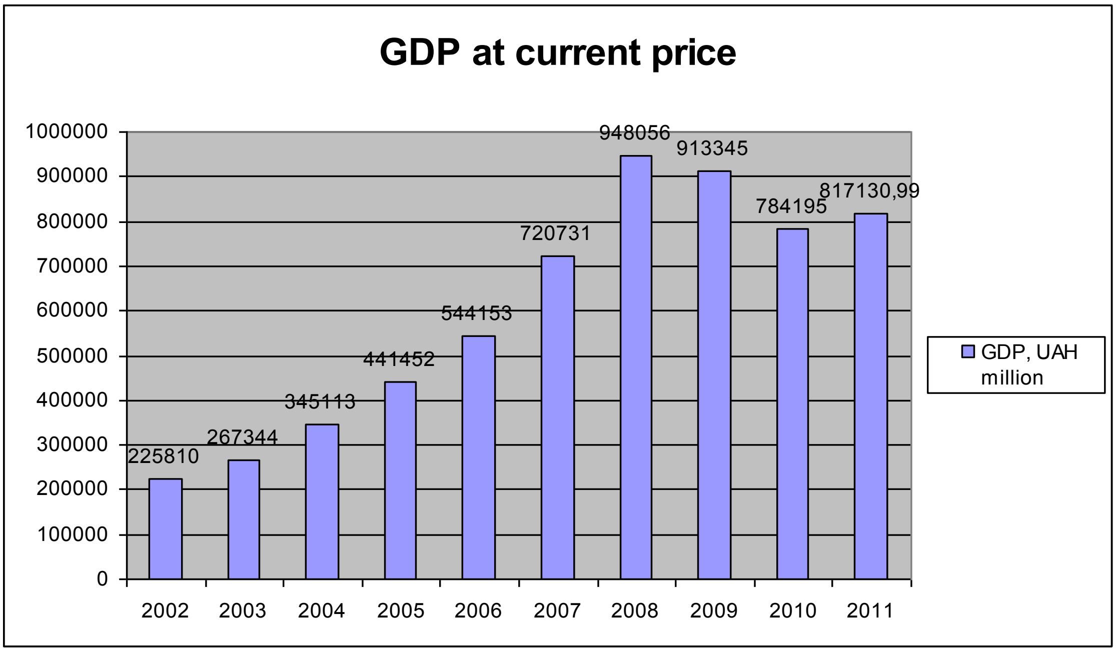
Effective reformation of economy of any country, structural transformation with the high-quality update of production processes and social infrastructure unthinkable without the proper capital investments. It is impossible to provide establishment and implementation of advanced technologies, development of market infrastructure without reliable capital investments [8].

In addition, the investment is to implement scientific and technological achievements in production and on this basis to ensure GDP growth, labor productivity, real income per capita, but also solve many social problems. Research has established a direct relationship between GDP growth and investment, for competitiveness and growth of enterprises defined investment. Without them the company of any form of ownership and doomed to failure.



From 2002 to 2008, the economy of Ukraine was on a steady rise. However, Gross Domestic Product (GDP) growth rate declined sharply in 2009, as a result of a decline in investments, low external demand and domestic demand. In 2009, the unfavourable economic conditions affected dynamics of most economic activities, except agriculture. Specifically, the largest decline was registered in fixed capital formation in GDP.

Research of problem of investing of economy always was in a spotlight economic idea. It is conditioned that investments touch the deepest bases of economic activity, determine the process of the economy growing on the whole. In modern terms they come forward a major backer-up exit conditions from an economic crisis, structural changes in economy, growth of technical progress, increase of high-quality economic performance indicators, on micro and macro levels. Activation of investment process is one of the most reliable mechanisms of socio-economic transformations



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The fixed capital investment in economic growth has been considered one of the basic principles in economics. FDI is of special interest for its supposed positive effects on growth. There is a widely accepted view that FDI promotes growth not only directly by augmenting capital formation in the recipient economy, but also indirectly by inducing human capital development, helping technology transfers and strengthening competition. Mainly for the sake of these potential merits of FDI, both developing and developed countries have become more receptive to FDI inflows, and the global FDI flows have continued to increase, except for a short-lived decline at the beginning of 2000s.

Even though Ukraine is the second largest European country in terms of population and geography, the amount of foreign investment its economy currently receives is considerably low. In comparison with Central European and Baltic states, Ukraine was slower to open its borders to trade and had difficulty attracting large inflows of FDI. The Ukrainian policy makers took a longer time to implement free market reforms and create the appropriate policy framework for foreign environment. Although, the government established a legal framework for privatization, widespread resistance to free market reforms from the Verhovna Rada delayed necessary reforms and led to some backtracking. The main directions of Ukraine's development are removal of structural deformations in development of economy and bringing in of modern technologies, able to show out the country on the trajectory of dynamic growth.

(FDI) are the most important part of global capital flows. FDI solve the important problems for the economy such as the output of innovative products for domestic and foreign markets, import substitution and transfer of industrial production to the stage of sustained economic growth. All this need to create favorable investment climate and conditions.

Ukraine is a large market with 46 million population. It has high potential and low level of competition in many sectors. Ukraine’s economy is on sustainable growth track. In 2011, the GPD had increase by 5,2% (in 2010 – by 4,3%), industrial output – by 7,6% (2010 – 11%) compared to previous year. The 2012 GDP growth forecast is up to 4%.

Key findings on Ukraine's FDI attractiveness:

- Europe’s share of actual FDI inflows was 26% (first place) in 2010, which is equal to its share of world GDP. However, Europe’s recovery remains mixed and tentative. [3]
- Ukraine ranks 10th in Central and Eastern Europe (2006–2010) for the number of FDI projects (178) and number of jobs created (7,487).

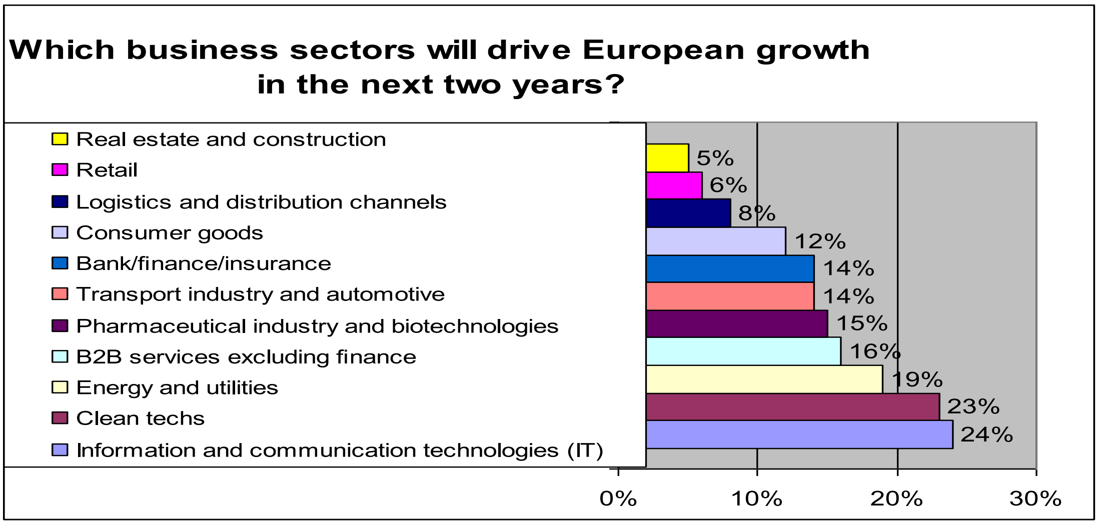
- In 2010 Ukraine attracted 31 projects and created 1,150 jobs.
- Ukraine is the 3rd largest recipient for FDI in financial services in Central and Eastern Europe (2006–2010).
- The Ukrainian industrial sector grew by 11.5% in 2010, but Ukraine attracted only 3% of all industrial FDI into Central and Eastern Europe.
- The largest investors in Ukraine are the USA, the EU countries and Russia.
- Reforms: investors expect improved infrastructure, increased stability and transparency, investment in talent and innovation [8].

We can observe during last year the improvements in the Investment Climate.

- The profit tax will be gradually reduced for all businesses from 23% in 2011 to 16% in 2014. The current 20% VAT rate will be reduced to 17% by 2014.
- Hotel business, alternative energy, light industry, ship building and agrarian machinery manufacturing are exempt from the profit tax for 10 year period (until 2020).
- In April, 2011, a package of anticorruption legislation was adopted by the parliament, aimed at reducing the corruption burden of businesses.
- Ukrainian Government has established a Council of National and International Investors, representing the Microsoft and other multinational companies [8].

The total FDI to Ukraine on April 1, 2012 amounted to 50 billion 793.5 million. To improve the macroeconomic stability of Ukraine the government initiated an aggressive reform program in 2010 to stabilize the Ukrainian sovereign debt position and as a result encourage growth prospects. The reform package includes: streamlining tax legislation, privatization of the energy sector and deregulation. Based on the current reforms, it looks likely that Ukraine will move up 23 to 33 points in the doing business ranking, but room for improvement remains.

Looking down the road, Ukraine should begin investing in talent and innovation to compete with European leaders in FDI. Investors clearly expect European growth to be driven by innovation-intensive sectors such as IT and clean technologies.



One of the advantages of FDI is that it helps in the economic development of the particular country where the investment is being made.

The National Bank of Ukraine reports optimistic statistics: in the third month of the year Ukraine’s balance of payments (BOP) became positive. [4]

In March 2012, the BOP surplus was $375 million, while in previous month it was negative $55 million. A year ago, in March 2011, the balance was negative $511 million.

These data were published by the National Bank of Ukraine on the 27th of April.

«Improvement in the balance of payments is caused, on the first place, by the decrease in the current account deficit to the level of $313 million in March (comparing to $1,3 billion in February). It is explained by the decrease in goods trading deficit ($893 million, comparing to $1,8 billion in February), and also by the inflow of significant dividends from foreign investments abroad», — says the Bank's statement.

In general, current account deficit in the first quarter was relatively low – $1,2 billion.

The National Bank also informs that the net capital inflow in March 2012 was $688 million (in March 2011 – net outflow was $102 million), in the first quarter – $640 million (the first quarter 2011 – inflow of $2,453 billion) [7].

The net inflow of the FDI to Ukraine in March was $127 million (in February – $832 million). The net FDI inflow to Ukraine in the first quarter of 2012 was $1,4 billion (January-March 2011 – $0,9 billion), which is 1,6 times higher comparing to the same period of the previous year [6].

The attraction and promotion of FDI is an important component of Ukraine's economic reform agenda. FDI could act as a motor for economic growth and welfare. Using the positive effects of FDI, Ukraine could catch up to the competitiveness level of the globally leading industrial economies much faster than by relying only on strengthening domestic firms. 'Could', because Ukraine's current stock of FDI is still too small and powerless.

FDI has provided capital to modernize obsolete factories and construct new ones. Foreign investors have often introduced modern technologies, more efficient managerial strategies, and more dynamic business practices. While the foreign investment may facilitate technology transfer, such transfer can sometimes be limited because new technology may not always be commercially available because innovating firms may refuse to sell their technologies via licensing agreements to the developing countries where they operate. Foreign investment does more than simply provide capital to local enterprises, it also diffuses useful knowledge and managerial skills which lead to higher productivity level of the domestic firms. Moreover, foreign investment also promotes the competition necessary to stimulate technology diffusion, particularly if local firms are protected from import competition. In many cases, multinational enterprises offer employee training programs in how to efficiently use new technology and adopt new marketing strategies. Further, technology diffusion often occurs through labor turnover as domestic employees move from foreign to domestic firms.

Despite the criticism that foreign investors often seek to exploit the local population and take advantage of cheap natural resources, multinational enterprises in general promote economic growth and raise wages for workers in the countries where they operate. The foreign-owned firms generally pay higher wages than domestic firms, leading to an increase in overall wages in the host county.

The Ukrainian economy would also benefit greatly from decreasing its dependence on Russian energy supplies, which the government can accomplish by promoting the diversification of energy suppliers and obtaining more FDI in the energy sector. In particular, the government needs to work on eliminating barriers which prohibit foreign investors from participating in the construction and ownership of new gas and oil transit pipelines.

FDI creates employment, especially if it is invested in Greenfield operations. Moreover, additional jobs may be created in local suppliers. FDI may also compensate local firms that use more labor-intensive methods of production and thus more employment.

FDI may help local firms to access export markets. Moreover, foreign investors may help building trade channels and a country of origin reputation that local followers may use for their exports.

Nowadays, with some confidence we can say that Ukraine, as a democratic state, has formed a monetary and banking system, a solid foundation for financial stabilization, which forms the basic conditions for development investment processes in Ukraine.

Priority areas for engagement and support of strategic investors can be identified, where Ukraine has a traditional production, possession of a necessary resource potential and creates a significant market demand for the products, namely: the production of cars and trucks, tractors; aircraft and rocket ; shipbuilding; vicious cycle of production of fuel for nuclear power plant, development of power generating facilities, oil and gas production, particularly in the Black Sea shelf, the introduction of resource and energy-saving technologies, agro-processing, transport infrastructure [5]. Effectively solve the problem of reducing resources and energy can only be through the widespread introduction of new technologies of modern technology, tied together by the interests of research and practice through market demand.

Despite the fact that Ukraine's investment climate is still maturing, foreign companies are successfully doing business in Ukraine. The more successful amongst them have adopted their business strategy to a changeable economic environment and have become familiar with having to forecast business and other risks which arise from time to time whilst engaged in the practice of business in the country.

Conclusions, proposals, recommendations

Many countries, including developing and transition economies have changed their attitude towards FDI over the past decade. Countries have liberalized their policies to attract rather than repel investment from multinational enterprises and they actually compete against one another by offering generous incentive packages. Furthermore, many developing countries have offered special tax incentives and subsidies to attract foreign capital, as it is strongly believed that FDI and portfolio inflows encourage technology transfers that accelerate overall economic growth. While there has been a growing acknowledgement of the role that direct investment can play in stimulating economic growth and development, there remains a tremendous diversity in approaches of countries in their policies towards FDI, as well as a kind of scepticism in certain spheres as to the inevitability or universality of the benefits from FDI. Ukraine has made a significant progress since the independence. It has established a functioning democracy with competitive elections, opened economy, a free media. No doubt, with a great investment potential of a vast emerging market of around fifty million consumers making it the greatest market in Eastern Europe, highly competitive, well-educated, skilled workforce and strategic location at the crossroads of East-West and North-South trade routes, rapid economic growth and European integration makes Ukraine very attractive destination for potential investments.

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