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THE ROLE OF UKRAINE IN THE INTERNATIONAL CAPITAL FLOW: CONDITIONS AND PERSPECTIVES

Abstract: Ukraine is an active member of international capital flow, but the capital import is sufficiently exceeds its export. The enhancing of Ukraine's participation in the international capital flow requires a creation of a favorable investment climate (tax remissions, legal security of investments), developing of an insurance system of foreign enterprises, improving of existing legislation in foreign trade sphere.

Keywords: international capital flow, trends, perspectives, new ways of solution, capital export, capital import.

Introduction

As the present international practice shows, the successful economic development is not possible without efficient international capital flows management.

From the political and economic points of view the international capital flows are the transfers of a relative surplus of capital over national borders for gaining the purpose using the productive, material and labor resources of the capital importing country.

The core of the global capital market is the Euromarket, a part of the worldwide capital market, where banks provide deposit and loan transactions in Eurocurrency (it functions as a loan capital outside the country of origin). Volume of loan capital within European markets is 7-8 trl. dollars. otal worldwide capital market volume is 10 trl. dollars.

1. Ukraine's place in the international capital flows

Global investment flows are increasing yearly, the geography of their widening is expanding, and Ukraine is an active participant in international capital flows. But in present socio-economic development conditions Ukraine takes a small place amongst the major European capital importing countries. The thing is that most of developed countries create the excess of capital that can be more profitably invested over their national borders in order to obtain the greater profit.

In practice, international capital flows are being materialized through investments. Export of the capital takes place in two main forms - business undertakings and loans. Export of business capital means investments to the industry, transport, farms, etc. through the constructing or the purchase of existing businesses by acquisition of their shares. This process leads to the formation of property abroad. Investments based on business capital exporting have two forms depending on the degree of real control over the activity of established enterprises:

- direct foreign investment is an investment in foreign enterprises which provides investors with direct control over them and the appropriate income. Direct control for the foreign investor over the enterprise is provided by obtaining of 100% share capital so as owning of the controlling interest (at least 25% equity, and for U.S. enterprises at least 10%).

- Portfolio foreign investment is an investment in a foreign company that brings investors an appropriate return, but doesn't give a right of control over enterprises.

Investment is important for both countries: exporter of capital receives profit, which may be used outside their residence country or otherwise for local investments. Importers of capital achieve the effective and efficient use of external sources of financing and technologies in their national interests.

The countries that export the capital, positive achievements are the expansion of markets for domestically produced goods and services, profit on investments, influence on foreign and internal policy of countries-importers, the benefits of deepening the international division of labor process, an access to cheap markets of labor. The negative consequences are worsening the national balance of trade, shortening the labor markets and amount of labor force in the national economy.

In recent years the countries of ex-Soviet Union camp started an engagement process of foreign direct investment, due to their significant effect to the economies transformation. These transformations lead to setting the market relationships within those economies and bring out the real way of implementing and use of modern techniques, technologies and management methods (Table 1).

Table 1 – The ratio of the amount of foreign direct investments from and into Ukraine in recent five years [1].

| Foreign direct investments | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 |
|---|-----------|----------|-----------|-----------|-----------|-------------|
| Foreign direct investments into Ukraine, mln USD | | | | | | |
| Capital of non-residents in Ukraine: | | | | | | |
| - the beginning of year | 9047.0 | 16890.0 | 21607.3 | 29542.7 | 35616.4 | 40053.0 |
| - the end of year | 16375.2 | 21503.3 | 29489.4 | 35723.4 | 40026.8 | 44708.0 |
| Aggregate capital of non-residents, including the loan capital | 17301.9 | 24476.1 | 33491.0 | 40957.4 | 46642.0 | 50607.3 |
| The share of loan capital in the total external funding, % | 5.36 | 12.5 | 11.95 | 12.82 | 14.19 | 11.66 |
| The growth rate of capital importing | | 1.87 | 1.36 | 1.36 | 1.21 | 1.12 |
| Foreign direct investments from Ukraine, mln USD | | | | | | |
| Capital of residents in foreign economies: | | | | | | |
| - the beginning of year | 198.614 | 218.171 | 243.3 | 6196.6 | 6203.1 | 6226.3 |
| - the end of year | 218.171 | 243.3 | 6196.1 | 6198.6 | 6223.3 | 6871.1 |
| Aggregate capital of residents, including the loan capital | 466.525 | 470.1 | 6319.5 | 6321.9 | 6346.7 | 7002.0 |
| The ratio of inward and outward flows of foreign investments, % | 97.0-13.0 | 97.4-2.6 | 82.4-17.6 | 85.0-15.0 | 86.3-13.7 | 86.46-15.54 |
| The growth rate of capital exporting | | 1.10 | 1.11 | 25.49 | 1.001 | 1.004 |

The following tendencies may be defined analyzing the data of Table 1:

Import of capital into Ukraine exceeds its export and that trend continues. Export of capital from the country ranges from 2.6% of imported capital in 2005 to 15.54% in 2010.

The following aims are being purposed in the capital exporting:

- the attempt to consolidate and control the activity of local foreign business and the part of local market and thus satisfy the economic and political interests in that region.

- gaining the business profit or an interests on the loan capital.

The country may receive from the foreign investment process the following preferences:

- new technologies at a relatively low costs of its implementing and as a result, new workplaces;
- an assistance to more rapid development of production;
- improvement of workers skills to introduce new technologies;
- usage of foreign experience in management;
- the budget filling.

The negative consequences of capital importing include:

- the foreign interference to the national banking;
- eventual uncontrolled removing of raw materials;
- limitation of political freedom of the country;
- capture of basic sectors of the economy by foreign capital;
- hidden removing of profits outwards the country (tax frauds).

The following conclusions that can be drawn from analyzing Table 1:

- The rate of capital import into Ukraine is reducing. Thus, from 2005 to the present time the rate of capital import into Ukraine fell from 1.87 to 1.12.
- Great share of direct and portfolio investment, followed by reducing of banking loans;

Thus, we can state that the positive effects of international capital flows for countries importing capital (such as Ukraine) are implementation of improved technology and equipment, advanced forms of production, reduced unemployment, foreign currency inflows, the accelerated development of the existing economic system or its improvement.

The negative consequences of these processes are gradual loss of control over some of businesses, industries, increasing foreign influence in the military-strategic and political interests [6, p. 365].

Twelve major investor countries, accounting for over 82.76% of total direct investments coming into Ukraine are: Cyprus - 9914.6 mln.USD, Germany - 7076.9 mln.USD, Netherlands – 4707.8 mln.USD., Russian Federation - 3402.8 mln.USD, Austria - 2658.2 mln.USD, United Kingdom - 2298.8 mln.USD, France - 2367.1 mln.USD, British Virgin Islands, - 1460.8 mln.USD, Sweden - 1729.9 mln.USD and the United States - 1192.4 mln.USD, Italy - 982.4 mln.USD, Poland - 935.8 mln.USD. (Table 2). [1-5].

Table 2 –Foreign direct investments into Ukraine divided by the countries [1-5].

| Foreign direct investments into Ukraine divided by the countries, amount, mln.USD weight, % | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 |
|---|------------------------|------------------------|------------------------|------------------------------|------------------------|------------------------|-------------------------|
| Total | <u>9047.0</u> 100% | <u>16890.0</u> 100% | <u>21607.3</u> 100% | <u>29542.7</u> 100% | <u>35616.4</u> 100% | <u>40053.0</u> 100% | <u>44708.0</u> 100% |
| Cyprus | <u>1101.4</u> 12.18 | <u>1635.9</u> 9.69 | <u>3187.5</u> 14.75 | <u>5946.6</u> 20.13 | <u>7646.2</u> 21.47 | <u>9005.3</u> 22.48 | <u>9914.6</u> 22.18 |
| Germany | <u>653.7</u> 7.23 | <u>5503.7</u> 32.58 | <u>5578.1</u> 25.81 | <u>5918.3</u> 20.03 | <u>6393.0</u> 17.95 | <u>6601.9</u> 16.48 | <u>7076.9</u> 15.83 |
| Netherlands | <u>637.2</u> 7.04 | <u>919.5</u> 5.44 | <u>1533.8</u> 7.1 | <u>2508.8</u> 8.49 | <u>3197.4</u> 8.98 | <u>3954.5</u> 9.87 | <u>4707.8</u> 10.53 |
| Russian Federation | <u>720.8</u> 7.97 | <u>835.8</u> 4.95 | <u>1002.1</u> 4.64 | <u>1462.4</u> <u>4.95</u> | <u>1847.2</u> 5.18 | <u>2566.4</u> 6.41 | <u>3402.8</u> 7.61 |
| Austria | <u>361.1</u> 3.99 | <u>1439.5</u> 8.52 | <u>1633.7</u> 7.56 | <u>2067.4</u> 7.0 | <u>2443.8</u> 6.86 | <u>2605.2</u> 6.51 | <u>2658.2</u> 5.95 |
| France | <u>79.0</u> 0.87 | <u>87.9</u> 0.52 | <u>30.3</u> 0.14 | <u>1044.8</u> 3.54 | <u>1231.2</u> 3.46 | <u>1630.8</u> 4.07 | <u>2367.1</u> 5.29 |
| United Kingdom | <u>955.4</u> 10.56 | <u>1174.8</u> 6.96 | <u>1563.4</u> 7.24 | <u>1975.5</u> 6.69 | <u>2249.8</u> 6.32 | <u>2307.5</u> 5.76 | <u>2298.8</u> 5.14 |
| USA | <u>1190.6</u> 13.16 | <u>1387.4</u> 8.21 | <u>1396.8</u> 6.46 | <u>1430.1</u> 4.84 | <u>1464.6</u> 4.11 | <u>1309.1</u> 3.27 | <u>1192.4</u> 2.67 |
| Poland | <u>194.7</u> 2.15 | <u>225.5</u> 1.34 | <u>394.6</u> 1.83 | <u>672.1</u> 2.28 | <u>690.1</u> 1.94 | <u>866.7</u> 2.16 | <u>935.8</u> 2.09 |
| Other countries | <u>3153.1</u> 34.85 | <u>3680.0</u> 21.79 | <u>5287</u> 24.47 | <u>6516.7</u> 22.05 | <u>8453.1</u> 23.73 | <u>9205.6</u> 22.99 | <u>10153.6</u> 22.71 |

The analysis of Table 2 data determines the uneven flow of external financing in the territorial distribution. The greatest investor of Ukraine is Cyprus, with the share of investments increased by 2.3 times for the last 5 years. The second largest investor into Ukraine, Germany, increased its presence in Ukraine in 2.19 times. Countries that increase foreign direct investment into Ukraine include the Netherlands, Austria and France. Russia reduces the amount of foreign investment to Ukraine in percentage terms. The same trend is kept by the United States.

Table 3 Foreign direct Investment into Ukraine by the type of industry [1-5].

| Foreign direct Investment into Ukraine by the type of industry | | | | | | |
|--|---------|--------------|----------|--------------|----------|--------------|
| | mln.usd | weight, % | mln.usd. | weight, % | mln.usd. | weight, % |
| Total | 16375.2 | 100 | 35723.4 | 100 | 44708 | 100 |
| Agriculture and forestry, hunting | 597.2 | 3.6 | 803.2 | 2.2 | 833.7 | 1.89 |
| Fisheries | 2.1 | 0 | 5.3 | 0 | 12.9 | 0 |
| Industry | 5056.4 | 30.9 | 8056.5 | 22.6 | 14042.6 | 31.4 |
| Construction | 387.2 | 2.4 | 2052.9 | 5.71 | 2339.2 | 5.2 |
| Wholesale and retail trade | 1953.5 | 11.9 | 3718.4 | 10.4 | 4764.5 | 10.7 |
| Hotels and restaurants | 282.5 | 1.7 | 412.9 | 1.2 | 458.3 | 1.0 |
| Transport and communications | 743.7 | 4.5 | 1281.0 | 3.6 | 1711.2 | 3.8 |
| Financial activities | 169.3 | 1.0 | 7154.8 | 20.02 | 15059.5 | 33.7 |
| Real Estate | 926.5 | 5.7 | 3570.7 | 10.0 | 4754.1 | 10.6 |
| Education | 34.1 | 0.2 | 13.3 | 0.08 | 16.8 | 0.1 |
| Health | 177.5 | 1.1 | 123.8 | 0.4 | 131.2 | 0.3 |
| Investments unallocated by the type | 6045.2 | 36.92 | 8530.6 | 23.88 | 584 | 1.31 |

If we consider the direction of foreign direct investment by economic activity (Table 3) we may define the following:

- growth of foreign direct investment in the industry is increasing, but very slowly (by 0.5% over the last 5 years) and stands at one third of all foreign direct investment;

- investments in foreign direct investment increase rapidly only to the companies engaged in financial activities (from 1.0% in 2005 to 33.7% of the total foreign investments into Ukraine in 2010).

Direct foreign investments from Ukraine also increased compared to last year (Table 4). Their geographical distribution has not changed, Cyprus received 92.31% of investments (Table 4).

| Capital of residents in foreign economies: <u>amount, mln.USD</u> weight, % | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 |
|---|---------|---------|-------|-------------|--------|--------|--------|
| Total | 198.614 | 218.171 | 243.3 | 6196.6 | 6203.1 | 6226.3 | 6871.1 |
| Cyprus | 2.0 | 2.1 | 10.3 | 5825.5 | 5826.1 | 5778.5 | 6342.5 |
| Russian Federation | 97.3 | 102.9 | 104.0 | 148.6 | 99.9 | 166.1 | 194.3 |
| Latvia | ... | ... | 3.5 | 30.7 | 31.6 | 31.9 | 87.9 |
| Poland | 21.1 | 21.3 | 24.2 | 30.1 | 46.9 | 49.4 | 49.1 |
| Georgia | ... | 2.2 | 2.9 | <u>28.5</u> | 26.9 | 32.4 | 31.1 |
| British Virgin Islands | ... | ... | 0.1 | 10.9 | 14.3 | 20.8 | 25.8 |
| Kazakhstan | ... | ... | 0.2 | 0.8 | 26.8 | 27.1 | 25.2 |
| Moldova | ... | 0.9 | 1.3 | 26.7 | 26.6 | 15.2 | 15.2 |
| Switzerland | 4.7 | 4.0 | 4.3 | 4.6 | 5.0 | 5.1 | 9.3 |
| Germany | 0.4 | 0.3 | 0.4 | 2.5 | 2.6 | 5.2 | 9.2 |
| Lithuania | 0.4 | 0.4 | 2.9 | 4.0 | ... | ... | ... |
| Armenia | ... | ... | ... | 12.8 | 13.5 | ... | ... |
| USA | 5.7 | 5.6 | 5.7 | 5.9 | 5.9 | 5.8 | 5.8 |
| Other countries | 32.0 | 47.1 | 45.3 | 32.3 | 35.7 | 39.5 | 22.7 |

According to the Law of Ukraine "State Statistics" information is confidential.

Although Ukraine annually increases its investments abroad, their amount still remains insufficient. The country is still of an importing kind. Therefore, Ukraine's priority should lie in creating the equity capital in order to stimulate the investment process and the further creation of surplus capital.

2. Advantages and drawbacks of foreign capital investment in Ukraine

Investors are attracted to Ukraine by:

- Favorable geographical position;
- Potentially large market;
- High-skilled labor force and its relative cheapness;
- Low exchange rate of national currency;
- The ability to remove earnings.

The reasons that hinder investments into Ukraine:

- Links of the ukrainian economy with the former Soviet republics;
- Imbalance in the economy;
- Undeveloped infrastructure;
- Non-convertable national currency;
- Insufficiently flexible taxation system;
- Low production culture;
- Disparity of administration forms to the international management;
- Economic and political instability, which leads to the corresponding risks.

3. The prospective of development of Ukraine's participation in international capital flow

The prospects of intensification of Ukraine's participation in the international movement of capital as follows:

- Creation of favorable investment climate (tax remissions, legal framework for investment);
- Promoting the investments into the key industries;
- Development of insurance system for foreign companies;
- An active role of government in the prevention and compensation of possible negative social consequences to the investment projects within the territory Ukraine;
- Create conditions to activate domestic business;
- Deepening of market reforms;
- Improvement of existing legislation in the sphere of foreign economic activity and control over its following.

Conclusion

To transform Ukraine from a developing country in the world exporters of capital opinion needed, above all, improving of existing legislation in the sphere of economic activity and create a favorable investment climate (tax remissions, legislative security of investments) for domestic and foreign investors.

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