

# CHAPTER 1

## CURRENT TRENDS IN ECONOMIC DEVELOPMENT

### UKRAINE'S INVESTMENT COOPERATION WITH THE EU: PROBLEMS AND PROSPECTS IN MODERN CONDITIONS OF ECONOMIC DEVELOPMENT

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**Abstract.** The article considers theoretical basis of investment cooperation, defines the category of international investment cooperation, defines the principles of attracting foreign direct investment from EU countries, and peculiarities for host countries. The necessity of attracting foreign investments into the national economy is substantiated. The study identified factors that affect investment cooperation and the volume of investment. The analyzed movement of investments between Ukraine and the EU in the sectoral breakdown of country in the last twenty years. The movement of investments between Ukraine and EU countries in the sectoral and country context for the last twenty years is analyzed. It is noted that the benefits of direct investment are inherent in both the recipient country and the investor country. The article outlines the benefits of investment cooperation for Ukraine and the EU. The main problems on the way to promoting effective investment cooperation are generalized. Analysis of investment flows and observations prove positive changes in investment cooperation, and it became especially noticeable with the election of the European vector of development of Ukraine's foreign economic relations and the signing of the Association Agreement between Ukraine and the EU. The projected data are calculated on the basis of statistical data on investment flows between Ukraine and the EU without taking into account external factors influencing economic development. The article states that the constructed trend coincides with the global trend of the world economy. Based on the analysis of investment cooperation between Ukraine and the EU, and to improve it the author proposes the creation of a register of economically and technically viable investment projects in accordance with the priority of development of economic sectors, with taking into account the national interests of all regions of the country, promoting the direction of foreign capital to those regions, sectors and projects that are most in need. Priority sectors for foreign investment have been identified, steps to improve investment cooperation between Ukraine and EU countries have been proposed, and ways to overcome obstacles to the movement of foreign direct investment have been identified in the article.

**Keywords:** international investment cooperation, foreign direct investment, economic growth, macroeconomic factors, economic sectors.

**JEL Classification** E27, F21, F62

**Formulas:** 0; **fig.:** 1; **tabl.:** 2; **bibl.:** 12

**Introduction.** Investment and investment cooperation play a leading role in the development of national economies. In the context of economic growth, foreign direct investment is of particular importance for developing countries and countries with economies in transition, because own investments are usually not enough. Such investments have an impact on structural changes in the economies of countries, on the sectoral development of national economies and on the volume of social production. World experience has shown that the optimal and efficient use of

investment is the shortest way to develop productive forces, and the economy as a whole. In the current conditions of continuing to reform the domestic economy, in terms of Ukraine's integration as an independent state into the world community, and in terms of the European integration vector of development, particularly important is the issue of cooperation with partner countries, including investment cooperation with the European Union. Ukraine, as a recipient country, desperately needs to attract foreign direct investment to rebuild its economy, as it lacks its own investment.

**Literature review.** International investment agreements are a key tool in economic development strategies for most developing countries and countries with economies in transition. UNCTAD experts conducted a study on the dependence of the impact of international investment agreements on investment inflows [1]. It is revealed that the recipient countries are reviewing the role of international investment agreements not only as a tool to stimulate FDI inflows from developed countries, but also as a tool to encourage and protect national investments, going to developed and other countries.

Manuel F. Montes and Adriano José Timossi in their scientific work considered the basic principles of reforming the regime of protect investment, including agreements and the system of settlement of disputes between investor and recipient in the context of South-South dialogue on future investment cooperation [2].

Loukas Mistelis and others consider international investment cooperation and investment agreements as a topical issue for the reform of recipient countries [3]. At the same time, they place emphasis on the reforms that should go beyond investment agreements and focus on promising projects of sustainable development, environmental protection, support for small and medium-sized businesses.

Falkner R. in his work focused on the peculiarities of investment cooperation, which requires an adjusting the behavior of entities to achieve mutually beneficial goals, and is a widespread in the world economy. It is noted that such management is based on the context of interaction, which is institutionalized and has a more permanent nature [4, pp. 72-74]. It is necessary to bring together the interests of actors in international investment cooperation through the coordination function of markets. It is also noted that the impact of globalization on the change in the structure of economic activity, the emergence of global production networks, form a demand in particular for investment resources. The growing demand for investment services has led to the development of institutional forms of investment cooperation between company's resident in different countries [5].

Many Ukrainian scholars consider the principles of international investment cooperation through the analysis of foreign investment between countries [6-9]. The raised issues in the scientific literature are relevant today.

**Aims.** Investigate the features of Ukraine's investment cooperation with EU member states in order to improve investment cooperation and probable prospects for development.

**Methods.** The main research methods were scientific abstraction, logical generalization, graphical method for determination projected data on investment

flows between Ukraine and the EU as a basis for improving international investment cooperation and national economic growth.

**Results.** International investment cooperation has been in active development since the last century. There is no unified and commonly accepted understanding of the category ‘international investment cooperation’. One understands this notion as various opportunities and forms of investment cooperation for all interested stakeholders-residents from different countries whose purpose is diversifying resources and distributing them efficiently, achieving set goals, obtaining income (profit), and useful effect. In the framework of investment cooperation various other forms of cooperation arise including production and technical cooperation (by this one means coordination and mutual long-standing production and technical activity of partners from different world countries based on allocation of production programs) and international scientific and technical cooperation manifesting itself through mutual solving of scientific and technical problems by partners from different countries, mutual exchange of production experience, mutual exchange of scientific achievements and mutual training of highly qualified personnel.

Investment cooperation of Ukraine with the EU countries is carried out by signing bilateral agreements. Thus, there are 23 agreements signed with the European countries. Such cooperation facilitates:

- establishing favourable conditions for investment at the level of both countries;
- expanding economic cooperation for the mutual benefit of both countries;
- intensifying cooperation between private enterprises at the level of both countries;
- the need to encouragement and security of foreign investments;
- as well as economic development of Ukraine and a EU member country.

There are macro economical factors influencing investment cooperation and the volume of investment movement between Ukraine and the EU countries: (I) factors of the sphere level and those of the micro level; (ii) objective and subjective factors. The objective factors include resources and economical, political and economical factors, global and economical, location of an object (territorial conditions), etc. The subjective factors include the state of the economy measured with macro economical indices (including the level of inflation, preconditions and the growth level of GDP, stability of the legislative system, interest rate level, etc.), taxation rates - availability of a clear and understandable taxation system, and market environment considered through the available infrastructure, openness of the economy, capacity of the internal market, etc.

So, all the factors mentioned above are an integral part in the flow of foreign investments between Ukraine and the EU countries. The major part of the European business activity in the last decade namely the European FDI has been directed into the following sectors [10]: financial and insurance activity – 27 %; production (mainly through privatization) – 25 % (from these 20 % are process manufacturing); wholesale and retail trade – 15 %; real estate operations – 10 %; food stuffs manufacturing, beverages, and nicotine products – 7 %; other– 16 %. Among the EU countries investors into the economy of Ukraine are Cyprus, the Netherlands, the

United Kingdom, the Virginian Islands (Great Britain), Germany, France, Austria, and Poland [11].

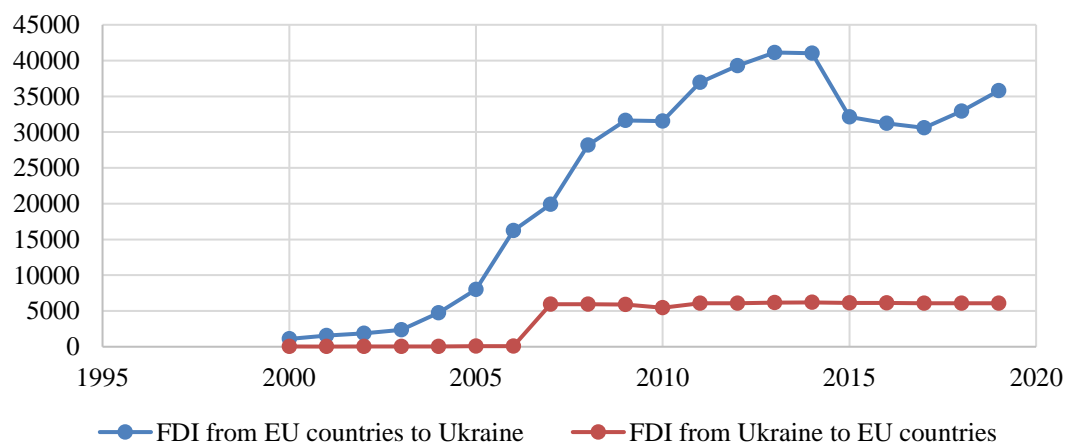
The following sector have always been attractive targets for foreign and European investors since Ukraine has become independent: wholesale and retail activity, financial, banking, and insurance activity, foodstuff production. The reason behind that is that it is these sectors which give the quickest return on investment and have relatively little risk for investors. The EU is interested in investing into the Ukrainian process manufacturing (the fifth part of all FDI). One can explain that with the inherent problem of lack of raw materials and energy resources typical for the EU economy [12].

In general, the advantages of direct investment are intrinsic both for Ukraine and the EU member countries. In particular, for European investors investment will facilitate the following:

- reduction and avoidance of quotas, tariffs for goods produced at the national market;
- diversification for the European capital flows, diversification of the European investors' activity;
- reduction of risks by signing bilateral agreements;
- developing the Ukrainian market thereby reducing transport costs;
- using highly trained work force which is relatively cheap reducing the final cost of goods produced at the national market for goods and services;
- obtaining additional income, profit, and dividends.

The advantages of European investment for Ukraine are as follows:

- mastering cutting edge and innovative technologies;
- additional workplaces and as a result lesser levels of workforce outflows, especially in the EU member countries;
- stimulation of the national economy with the help of European investment which in turn increase the GDP and economical growth. In turn European investment will not only improve cooperation but increase the efficacy of the national economy. The Investment cooperation between Ukraine and the EU member counties is constantly increasing as confirmed by the statistical data (Fig. 1).



**Figure 1. Investment flows between Ukraine and the EU, 2000-2019, mil. USD**

Source: author's development based on [10]

The investment cooperation between Ukraine and the EU should reflect not only modern trends of global economy and global processes of its development but their discrepancies in the world economy as well as positive facets.

There are following principal problems in the way of development and facilitation of effective investment cooperation: The level of corruption in the country, anti-corruption reforms, resolving the crisis of the Constitutional Court; difficult political climate, political strife directly influencing the implementation of the reform; the economic growth and macro economical indices; the current situation with the COVID 19 pandemic causing not only a reduction in the volume of foreign trade and loss of investors but leaves Ukraine vulnerable to outside shock and inventory cycle on the whole.

At the same time, taking into account the European vector of foreign economic connection of Ukraine, the signed Ukraine–European Union Association Agreement, there has been present a trend of improvement in investment cooperation. The author has plotted a dynamic of changes in the amount of European investment in Ukraine for the period of 2000-2019 and determined a further trend line using the graphic method (Fig. 1). Selection of the empirical function has been done by using linear, logarithmic, polynomial, and power functions.

**Table 1. Functions that determine investment trends between Ukraine and the EU, 2000-2019**

Function	FDI from EU countries to Ukraine	FDI from Ukraine to EU countries
Linear	$y = 2176,5x - 4E+06$ $R^2 = 0,7534$	$y = 416,11x - 832246$ $R^2 = 0,7062$
Power	$y = 0x^{363,14}$ $R^2 = 0,7279$	$y = 0x^{736,43}$ $R^2 = 0,7159$
Polynomial	$y = -179,85x^2 + 725012x - 7E+08$ $R^2 = 0,8892$	$y = -29,665x^2 + 119640x - 1E+08$ $R^2 = 0,801$
Logarithmic	$y = 4E+06\ln(x) - 3E+07$ $R^2 = 0,7542$	$y = 836555\ln(x) - 6E+06$ $R^2 = 0,7069$

Source: author's development

The trend of changes in FDI from the EU has been analysed using linear, logarithmic, polynomial, and power functions. At the figure the function maximally converge: linear ( $R^2=0,61$ ), logarithmic ( $R^2=0,61$ ), polynomial ( $R^2=0,67$ ), power ( $R^2=0,81$ ). The validity coefficient is the biggest for the power function; although, if we increase the determination coefficient, the calculations will have a higher validity coefficient. The bigger the polynomial, the higher the value of the validity coefficient.

Correspondingly, let us analyse a trend of FDI flow to the EU by using linear, logarithmic, polynomial, and power functions. The figure shows that the investment outflows from Ukraine to the EU functions maximally converge: linear ( $R^2=0,71$ ), logarithmic ( $R^2=0,71$ ), polynomial ( $R^2=0,72$ ), power ( $R^2=0,85$ ). The power function has the highest validity coefficient.

The value of the functions in both trends are close to unity which signifies the highest probability of the forecast values. Therefore, in the next four years the trend

will show a gradual growth. Figure 2 provides statistical data as to the investment flows for the last five years and contains a forecast for the next four years (save for unforeseeable factors, world crises, etc.) using the data available from the last twenty years. The said trend matches the world trend for the world economy development.

**Table 2. FDI trends between Ukraine and the EU for 2015-2019 and predictive values by 2024, million dollars USA**

Year	Direct investment in Ukraine			Direct investment from Ukraine		
	Total	from EU	% of EU countries	Total	to EU	% of EU countries
2015	32122,5	24982,8	77,8	6315,2	6111,0	96,8
2016	31230,3	23425,7	75,0	6346,3	6115,1	96,4
2017	31606,4	24145,2	76,4	6322,0	6075,5	96,1
2018	32905,1	25972,3	78,9	6294,4	6084,4	96,7
2019	35809,6	28289,3	79,0	6272,7	6086,0	97,0
Predictive values						
Year	from EU countries			to EU countries		
2021	46262,07			8293,147		
2022	48438,58			8709,255		
2023	50615,09			9125,363		
2024	52791,6			9541,472		

Source: author's development

In order to improve investment cooperation between Ukraine and the EU and to achieve the forecast values of investment flows and promote national economic growth, some efforts are needed. Such proposals may be, as noted by leading scientists and experts, the creation of a register of economically and technically viable investment projects in accordance with the priority of development of economic sectors. Of course, it is necessary to take into account the national interests of all regions of the country and to promote the direction of foreign capital to those regions, sectors and projects that are most in need. Therefore, we can support the selection of such groups to attract foreign capital in the first place:

1. The most vital industries, which are not only a priority, but also important for the economy of Ukraine include transport, engineering and electricity.

2. The second group consists of sectors of the economy that are also important for the economies of Ukraine. Enterprises in these industries can survive and become competitive in today's conditions of trade liberalization and liberalization of foreign economic relations and it can help update technology and increase the efficiency of production. These include ferrous and nonferrous metallurgy, enterprises of the military-industrial complex, and chemical industry.

3. The third group includes enterprises that are not competitive today, and may even be unprofitable. This group includes coal companies, agriculture, civil engineering, production of chemical fibers and plastics and others. They are the ones most in need of investment, new approaches in the organization of production and technology upgrades.

Also, in order to improve investment cooperation and relations between Ukraine and the EU, the main priority steps should be the following: establishing investment cooperation in the context of Ukraine's European strategy and strategic programs; introduction of forms of international joint financing of strategic investment projects; formation of a system of mutual protection of investments; promoting investment in priority sectors of the economy; supporting through economic diplomacy for the creation of consortia, alliances of Ukrainian enterprises with powerful European companies; dissemination of information on investment demand and opportunities in domestic production and economic sectors; introduction of monitoring of pricing within TNCs, in order to prevent tax evasion in Ukraine.

**Conclusion.** The foreign direct investment market is characterized by the intensive development of globalization, strengthening the interdependence of the world's economies, including strengthening investment cooperation between Ukraine and the EU. Increasing the level of confidence of foreign investors, improving and strengthening of investment cooperation with European countries, and cooperation with international creditors is important for national needs for strengthening international reserves, investing in critical sectors and national projects, and economic growth in general.

Having identified priority sectors and priority steps for attracting foreign investment, and analyzing approaches to investing in the EU we can note that effective cooperation between Ukraine and the countries of the European Union is possible even under the conditions of first of all adaptation of the domestic legislation on the European one. Ukraine must comply with certain EU directives in the field of investment, in particular, for example, on the transparency of securities and on compensation for losses to foreign investors. Therefore, the legal framework must be improved, and must be transparent, clear and one-sided for European investors, and protect the rights of foreign investors.

What does Ukraine need to do to overcome obstacles in order to attract European investors? In the context of the European integration vector chosen by the government, in addition to the above steps, it is also necessary to modernize the sphere of investment activity, namely to develop adequate and effective incentive policy measures. Stimulation attracting of European investments, infrastructure of investment activity, formation of an attractive investment environment should become a priority in investment activity. To achieve this goal, it is necessary to use world experience and to use those stimulating and possible factors that will contribute to the implementation of the country's investment policy. Such measures will confirm the positive forecast trends that we have calculated.

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