



Ukraine



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SESSION 3: INVESTMENT, ENTREPRENEURSHIP AND REGIONAL DEVELOPMENT

Summary of recommendations and issues for discussion¹

In the context of transition, effective regional/local development policy is crucial to the success of wider reforms. Strong regional disparities and resulting economic and social implications can hamper or delay the implementation of reforms and sectoral policies. Rapid restructuring can exacerbate traditional regional gaps (e.g. between urban and rural regions) and create new disparities. Once prosperous heavily industrialised regions can find themselves in decline, whilst other areas rapidly advance towards “new” prosperity. Designing a regional development policy that can successfully address these challenges is not an easy task. Not only should it try to even out the regional unbalances in the transition, but also define policies and tools that tackle the different structural problems: plant closures and industrial restructuring, economic decline and conversion, rural depression, social exclusion and joblessness. Whilst central governments pull the macro-economic levers, interventions at city or regional level can enhance the beneficial (or remediate the negative) impacts of the macro changes and the higher tier policies. The capacity of cities and regions to develop and implement effective development strategies becomes vital to harnessing indigenous strengths, contributing to national growth and levelling regional disparities.

Within the framework of the OECD-EC initiative on “Improving the Conditions for Enterprise Development and the Investment Climate for Domestic and International Investors in Ukraine”, several activities have been undertaken at regional level in Ukraine in order to analyse current practices and provide policy recommendations to local and regional administrations and central government authorities in the following fields:

- FDI and regional development (the case of Lviv region);
- Industrial restructuring and enterprise development at regional level (the case of Kharkiv region);
- Investment and entrepreneurship development in the tourism sector (the case of the Republic of Crimea).

¹ The discussions will mainly focus on FDI and regional development issue based on the results of the study on Lviv regional FDI policy. Materials on the other two themes will be available for information.

Overall, a co-ordinated effort by national and regional authorities is needed to address the following priority:

Ukraine regions should develop coherent, integrated development strategies based on an in-depth understanding and knowledge of local assets, competitive advantages and opportunities, which are aligned and co-ordinated with national growth objectives. Regional investment promotion and entrepreneurship development efforts must result from and help achieve national and regional economic and social development goals.

Participants of the round table are invited to give their reaction to the recommendations; specify what their agencies could do to help implement the recommendations; and provide their views on priorities for the future.

1. FDI and regional development: the case of Lviv region

Foreign direct investment (FDI) can play a major role in driving regional economic growth and creating employment in Ukrainian regions. FDI projects can bring important multiplier effects resulting from local procurement of materials and services and local spending of wages and salaries and a series of other benefits including technology transfers, upgrading the efficiency of local suppliers, competitors and customers, contributions to local infrastructure and improved labour force skills. However, regions risk losing potential investment and failing to secure the long-term development potential that FDI could represent because of a lack of effective policies to attract, retain and exploit FDI. The OECD study on FDI policy in the Lviv region, undertaken 2004-2005, examined the following issues:

- *FDI attraction*: Which aspects of the local environment regional authorities/agencies should build and market in order to attract appropriate foreign investment and how they should go about this marketing?
- *FDI aftercare and embedding*: How should public agencies deal with foreign investors once they have made their investment decision to reduce the chances of relocation elsewhere and maximise the chances of securing future expansions and related investments? How can they secure indirect benefits from foreign investment for example through local purchasing and technology transfer?

Based on this analysis, the study provides policy recommendations to Lviv regional and local authorities and development agencies that can be summarised as follows:

Develop and implement a coherent FDI attraction policy, building on the general economic development strategy, but specific and focused on the FDI market opportunities and region's competitive positioning. The following steps can be undertaken:

- *Identifying directions for FDI strategy*: Develop an overall FDI strategy jointly with all concerned stakeholders; Identify realistic FDI objectives; Inform the public about the strategy.
- *Setting targets for FDI attraction*: Analyse and monitor key FDI indicators on competitor locations, key source markets, and potential foreign investors; Evaluate the region's competitive position; Identify sector, market and company targets.
- *Organising FDI attraction*: Set up a "one-stop-shop" for FDI attraction, co-ordinating the activities of all bodies concerned; Plan and allocate necessary resources for FDI attraction; Identify policy actions to take.
- *Implementing FDI attraction strategy*: Improve the business environment for FDI, including human resources development, infrastructure and property development; Launch effective marketing and promotion tools; Undertake company targeting, lead generation, relationship building and account management.

Design an FDI aftercare policy to bring the maximum net economic benefit to the host region in the long run. The most appropriate focus for aftercare should be on types of strategic FDI which are mobile and contestable across national borders and whose economic impacts (direct, indirect and induced) are strongly additional and whose displacements effects are minimal.

- At regional level, first focus on supporting the bedding down of the initial investment projects to ensure that full project roll-out is achieved efficiently and to schedule. This is especially important if the planned number of jobs associated with these investments is to be fully realised.
- Respond to the key concerns of strategic investors related to the consistency and transparency of the application of Ukrainian regulations. These concerns relate to customs and excise; tax and social security; building and land approvals; anti-competitive practices; improvements in transport, telecommunications and utilities.

Support FDI embedding in the local economy by:

- Stimulating inter-firm alliances and networking between firms and research institutions in order to stimulate diffusion of new technologies and innovation.
- Promoting entrepreneurship and SME development to build or strengthen the supplier industries in the host region.
- Strengthening linkages between business and research by modifying the academic curriculum of local universities in accordance with the changing needs of the economy.
- Supporting the development of specialised clusters including the infrastructure and supply of trained human resources.

2. Industrial restructuring and enterprise development at regional level: the case of Kharkiv region

Industrial restructuring is often associated with its immediate negative effects on employment and high costs for the local or regional economy. Yet, in many cases, restructuring of enterprises is often crucial to their survival and can enhance the competitiveness of the local economy. While national governments determine the legal and institutional framework conditions for restructuring, it is at regional and local levels that industrial restructuring operations are most effectively managed. The central governments are instrumental in facilitating labour mobility; in setting rules and regulations related to entrepreneurship (e.g. easy market entry and exit conditions could facilitate the emergence of new enterprises capable of taking over the “non-core” production lines and absorbing the employees made redundant). At the same time, it is at local level that the restructuring effects are most deeply felt, particularly when large enterprises are concerned, or in the case of single-industry areas. It is the role of regional and local governments to effectively alleviate the negative effects of industrial restructuring.

Kharkiv’s region industrial restructuring efforts have been analysed at the OECD seminar held in 2005 which helped identify mechanisms for regional and local policy-makers aiming at improving business climate and encouraging the creation of sound jobs in economically viable enterprises. These recommendations can be summarised as follow.

- **Assess region’s strengths and comparative advantages** in order to refine policy measures geared towards the encouragement of private investment initiatives and to determine priorities for public investment in infrastructure and in supporting services.
- **Create an environment for growth by translating research into commerce:** support the process of developing new start-up businesses driven by the wide range of academic specialisations offered by Kharkiv’s universities and technical colleges; provide assistance to the spinning-off of technical subsidiaries from existing manufacturing facilities, as has already been done in some cases such as the Malyshev tank factory.
- **Improve the co-ordination and integration of regional public programmes on skills, training, labour market and regional economic development.** Consider to introduce area-based partnerships as a tool for improved local governance and co-ordination and adaptation of public policies to local conditions, needs and business development priorities.
- **Continue to address real estate issues** and the large deficits in industrial space, modern warehousing of a standard required for up-to-date logistics companies by: undertaking clean-up and reclamation work on redundant industrial sites which would result in the realisation of value in public land that has no value until reclamation work has been completed, and the creation of attractive sites which can either be sold or leased to private investors; or can be used to host industrial parks.

3. Investment and entrepreneurship development in the tourism sector: the case of the Autonomous Republic of Crimea

Tourism can be one of important drivers of regional development and job creation. However, if not aligned with broader long-term regional development strategies, it can also negatively impact on the local environment and destroy local identity. Efforts have to be made by regional and national policy makers to reconcile the competitiveness and quality of tourism industry and the pursuit of sustainable development objectives of regions and localities.

Tourism in the Crimea is well developed and forms the backbone of the region's economy. However, since the collapse of the Soviet Union the underlying demand conditions for the industry have changed, and there is evidence that the sector is being left behind in international competitive terms. The following measures, developed at a workshop held in Yalta, Crimea, in 2005, could help address this challenge.

- **Improve knowledge of origin markets:** detailed research in each of these main markets should be undertaken in order to prepare specific plans for their development and provide a backdrop against which more detailed tourism development policies can be prepared.
- **Product development:** review the tourism product inventory in order to identify specific areas where new investment might either open up market opportunities to develop new types of tourism in the region and/or develop new tourism products related to market potential.
- **Competitiveness and benchmarking:** undertake a review of those areas of the industry that would benefit from an international benchmarking exercise and take the steps necessary to seek the support to have such an exercise carried out.
- **Training programme:** training at all levels of the tourism industry is necessary to raise standards in the industry and thus help ensure the competitiveness of the tourism sector in the Crimea
- **Industry organisation:** Consider upgrading the institutional structure supporting Crimea's tourism sector. On the basis of existing structures a regional tourism authority could be created to develop a practical and tourism master plan covering a period of at least ten years, and to take direct responsibility for its implementation.