

The Role of the Financial Sector in Attracting FDI

Summary of recommendations and
issues for discussion

Ewa Sadowska-Cieslak

The Mission of the State Authorities Concerning Financial Sector is

- To create the right conditions for development of the effective and secure conversion of the savings of the population into the investment and local business financing,
- To support the development of the financial markets by setting up regulations and institutions,
- To attract the country to foreign investors who may bring additional financing and help accelerate the investment process and the economic growth of the country as end-effect,
- To safeguard the financial system stability

The discussions concentrated on:

- The basic pillars of favourable investment climate and their relevance to the financial sector,
- Liberalization of capital movements as a base for attracting foreign investment
- Financial sector stability issues,
- The problems facing both the banking and financial markets in Ukraine

Ukraine has been a weak competitor on the international market for investment capital.

- The highest inflows amounted to US\$ 1.7 billion in the year 2004 showing a two-fold increase in comparison with 2002
- Kazakhstan attracted US\$ 4.2 billion in 2004, Poland got US\$ 6.3 billion and Hungary attracted US\$ 4.1 billion
- FDI stock level in Ukraine amounted to US\$ 9.2 billion in 2004 while the same for Poland reached US\$ 61.4 billion and for Hungary US\$ 60 billion

Over 70% of the Total FDI World Inflows Have Been Located in the OECD Countries

- WHY?
- Because through out many years the OECD has developed the standards for international investors, which simplified the investment process and protect the investment.

The aim of the Ukrainian government is to fourfold investment and double the GDP by 2015

- If so, implementing the above mentioned standards will be the key issue for the coming years.

The three pillars of the favorable investment climate are:

- Economic and political stability (the economic even on the low level, but stable)
- Clear and stable legal framework
- Friendly business environment (financial sector creates one part of this climate)

Investors expect

- Freedom for cross-border capital movements (so called liberalization)- which however, may entail risk for financial stability of the country.
- At the same time they are interested in places for their investment which can offer long-term stability in terms of avoiding both, foreign exchange and financial crises.

What Means the Financial Stability in the Open Market Economy?

- The set of policies and institutions designed to prevent or reverse widespread disintermediation from banks, losses in bank capital, and bank failures constitute the safety net system.

Financial stability

- responsibilities must be shared among
 - The central bank
 - Institutions responsible for prudential supervision
 - Deposits guarantee funds

Ukraine's financial sector remained poorly developed by international standards which foreign investors are used to

- It is still relatively weak and needs further development to support the expanding economy.
- There is a strong potential for the deepening of capital markets provided adequate regulatory environment and strong institutions are provided.

Foreign direct investment

- Push the financial sector reforms by bringing capital, new technologies and know how.
- And the modernized financial sector adds to the friendly investment climate.
- It is a two-way process beneficial for the whole economy.

Challenges facing financial sector in the transition to a market economy:

- Implementing international standards into local legislation
- Building institutions
- Training employees,
- Educating society,
- Integrating into international financial organizations

*The real difficulty lies not in
developing new ideas but in
escaping from the old ones.*

J.M.Keynes