

## **Doing Business in Ukraine: Experiences of Australian Companies<sup>1</sup>**

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### **Abstract**

Although bilateral business relations between Australia and Ukraine during the past two decades are relatively minimal, the recent peak in trade between the two countries raises the question about the future of greater economic cooperation. The objective of this paper is to provide an empirical examination of the differences in the business environments of Australia and Ukraine and how they could undermine the potential for further development of these relations. The aim is to explore the risks that Australian businesses experience while operating in non-traditional markets and the motivation to engage in such a highly volatile business environment. Twelve in depth interviews were conducted, of which nine were companies involved in business between Australia and Ukraine as well as three individuals who closely participate in fostering the bilateral business relations.

**Keywords:** Trade, Investment, Australia, Ukraine, Economic Relations

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## **1. INTRODUCTION**

This paper investigates barriers to a greater economic cooperation between Australia and Ukraine. It is clear that by strengthening the ties between the two countries, both Ukraine and Australia, can further stimulate the growth of their economies. Australian companies express strong interest in the business opportunities available in Ukraine, which indicates that there is a strong potential for bilateral business relations. In fact, Australian and Ukrainian businesses can share their knowledge and experience in order to achieve a greater competitive advantage on the international arena. It is clear that business activities with Ukraine have been increasing noticeably since 1998, moreover, the recent peak of 340% in commodity turnover again illustrates a very strong potential that both countries can offer. Nevertheless, it is important to examine the recent deterioration in business relations between Australia and Ukraine. Furthermore, it is necessary to answer whether the growth in trade is sustainable. This paper examines the barriers to bilateral business relations in light of the specifics of the two business environments. This area of research is relatively new and there is yet no attempt to deepen the understanding of the business relations between the two countries.

This paper addresses the main issues that Australian companies face while conducting business activities with Ukraine. These issues are also examined from the perspective of the Ukrainian businesses that cooperate with the Australian firms. It is evident that there are significant risks, which are often underestimated by the Australian businesses prior to entering the Ukrainian market. There is significant opportunity offered in Ukraine, but at the same time there are numerous hidden rules that Australian businesses should be aware of. This issue should not be taken for granted, as all participants of this study identify that the business environment in Ukraine is highly volatile and unstable. In the same vein, the rules are very dynamic which often causes the risks to become unbearable.

The purpose of this paper is to provide a detailed investigation into the context of business relations with Ukraine. This paper allows businesses to explore and learn from the experiences of companies that are conducting operations between Australia and Ukraine. Understanding the specifics of the Ukrainian business environment will assist in the development of new successful business ties with Australia. This would be of great significance to business practitioners, policymakers and scholars in general, as the erudition about economic, legal and political factors that influence internationalisation process is vital not only for individual businesses but also to the advancement of the country as a whole.

To achieve the objective of this paper, three main research questions have been formulated as follows:

1. What is the potential for greater economic cooperation between Australia and Ukraine?
2. What are the main barriers to bilateral business relations between Australia and Ukraine?
3. How can the current risks and obstacles for business activity between the two countries be minimised?

First, this paper introduces a brief overview of the literature related to the internationalisation theories and provides a detailed discussion on the development of business relations between Australia and Ukraine. The emphasis is on Ukraine with an in-depth analysis of the macroeconomic performance, political developments as well as an outline on recent trade and investment statistics. Second, the use of Grounded Theory is justified in light of the purpose of this study; furthermore, a description of the sample is provided with necessary contextual details. Third, the paper illustrates the potential for business activities between Australia and Ukraine, provides a detailed examination of the barriers and obstacles between the two countries and makes relevant recommendations. Finally, study limitations are addressed and appropriate conclusions presented.

## **2. SELECTED BACKGROUND LITERATURE**

### **2.1 Selected Internationalisation Process Literature**

The Uppsala model of internationalisation attempts to explain motives to expand offshore. The model is constructed by using behavioural theory and the theory of the growth of the firm (Johanson and Vahlne 1977, 1990). The Uppsala model describes internationalisation as a *gradual* process where the firm by increasing its knowledge of foreign market will commit greater resources to operate in that marketplace. Nevertheless, the model is criticised on the grounds that the firm has to go through specific steps while internationalising (Reid 1983). These steps include the choice of the entry mode, which in part will be determined by the risks of the offshore environment. Another criticism of the Uppsala model is that at a later stage of internationalisation, when entering into a new market, a firm would not need to repeat the same steps of the process. Forsgren (2002) refers to the concept of learning and argues that when the firm already established offshore operations in one market it will apply its experiences to another.

The motivation to engage in internationalisation process varies across different firms. Firstly, in order to proceed with internationalisation strategy the company should have significant motivation or benefit. As argued by Brooks and Rosson (1982) excess capacity is

a significant internal motivator to expand operations offshore. Similarly, Johnston and Czinkota (1982) argue that firms can achieve marketing or technological advantage with internationalisation. External factors, such as profit maximisation, access to resources, that guarantee competitive advantage of the firm, are explained in Czinkota and Ronkainen (2001). It is argued that companies will consider internationalisation as a response to changing market conditions. Internationalisation is an instrument to achieve a greater competitive advantage, larger economies of scale as well as gain access to location-specific resources.

## **2.2 Selected Market Entry Mode Literature**

Since this study will provide recommendations on the entry mode into the Ukrainian market it is necessary to provide a brief discussion of the major theories of international entry mode. The internationalisation theory is a poor explanation of the entry mode choice, mainly because it assumes perfect competition, homogenous firms and mobility of resources, and thus far from today's real business environment (Ekeledo and Sivakumar 2004). Dunning's eclectic paradigm theory is meant to address the shortcomings of internationalisation theory, however, it is still criticised on the basis that it does not fully explain the entry mode choices by the firms (Dunning 1993). The resource-based theory, on the other hand, can provide an explanation not only to why different entry modes are chosen within the industry, but also illustrate why all firms within the same industry cannot choose the strategies that can offer the highest returns (Ekeledo and Sivakumar 2004). The resource-based approach argues that the firm will achieve its highest performance when there is a good fit between firm-specific resources and external opportunities (Conner 1991). Therefore, the firm's resources will be the main drivers of the business strategy.

## **3. RESEARCH CONTEXT**

### **3.1 Potential for greater economic cooperation between Australia and Ukraine**

Ukraine has been viewed as a new-coming state with relatively great potential ever since its independence. The industrial capacity of Ukraine demonstrates the potential for delivering goods and services that are in demand by the Australian economy, Ukraine is also regarded as a prospective market for the Australian exporters (Maley 1995). One of the major obstacles, however, was to leave the baggage of the command economy and respond to the demands of international and domestic markets. It can be stated that Ukrainian economy still remains at its transitional state. The business environment of Ukraine lacks transparency, as a

result, international actors find it difficult to estimate the risks prior to entering the market or establishing its operations in Ukraine.

Starting from early 1990s the lack of an independent image on the international arena was a detrimental factor for Ukraine. From the Australian perspective Ukraine was always viewed as part of the Soviet Union, even though, its existence under the communist regime was not a soothing experience. Australia recognised Ukraine as an independent state in December 1991, four months after it separated from the Soviet Union (Hill 1995). Ukraine is ranked as the largest country in Europe in terms of area and the seventh largest in terms of population. After the split from the Soviet Union Ukraine was the sixth largest economy in the world, ahead of China and Canada (Hill 1995). Ukraine also has significant mineral deposits, such as manganese, titanium, coal as well as oil and gas deposits. It is necessary to emphasise agricultural capabilities of Ukraine, as it supplied the former Soviet Union significant outputs of sugar, potato and grain. The industry was also well developed, especially in the area of metallurgy, machinery, chemistry and electronics. Ukraine also remains one of the leading countries in the field of space and aeronautic technology. Antonov aircraft factory currently is the only manufacturer of the world's largest cargo aircraft and also successfully supplies regional passenger aircraft to Russia, Asia, Africa and South America (Marson 2009).

Hill (1995) illustrates that the outcome of the economic reform will determine whether or not Ukraine will be able to utilise its full potential. It is argued that privatisation program will assist in moving away from the centralised government control which lacks the understanding of business and infrastructure. While it is over 15 years since the introduction of the economic reforms under Kravchuk, it cannot be stated that the development of businesses is free from government intervention which still places major obstacles to the business progress. The issue of overregulation will be addressed later in relevance to the reports by the World Bank and the Organisation for Economic Co-operation and Development (Refer to Section 6.3.1.3).

Ukraine and Australia can cooperate in the development of agriculture. In early 1990s textile mills in Ukraine were highly dependent on the Australian wool supplies (Helmer 1991). At the same time Australia had an overstock of wool which had to be processed. The purchase of Australian wool in 1991-92 was largely dependent on the credit arrangements established by the Australian Government through the Export and Finance Insurance Cooperation. Hills (1995) also argues that Australia can contribute to the development of the mining industry in Ukraine. Australia, as well as other developed

counties, could provide necessary technology and expertise in explorations of oil and gas deposits, modernisation of energy sector and coal industry. This paper will later provide a detailed examination of the debate between OilExplore and Ukrnafta, which further illustrates the point (Refer to Section 5.2.1 and Section 6).

In early 1990s Ukraine needed investment into the agricultural infrastructure, especially storage, and transport system that would prevent the losses in harvesting, storage and handling (Hill 1995). Nevertheless, it remains a problematic issue. In 2007-08 Ukraine was losing a significant amount of grain due to poor infrastructure and export quotas (ABB Grain Ltd., notes from the presentation on 22<sup>nd</sup> November 2008). The debate in early 1990s outlined that foreign investment and joint ventures is the most effective way to assist the development of the new economy. The average life of industrial fixed assets in Ukraine during early 1990s was exceeding not only the norms in western countries but also the standards of the former Soviet Union (Serbin 1991). It should be stressed that the lag of infrastructure development remains a significant issue that is still evident today.

ABB Grain's joint venture with Soufflet, New World Grain, is an example how the Australian involvement can stimulate the growth of the economies of the two countries. Section 6 will assess the operations of New World Grain in light of the obstacles and benefits that the company experienced during its operations in the Ukrainian business environment.

During 2004-2007 Australian businesses viewed Ukraine as a country with great business opportunities. Ukraine has 47 million people with growing medium class merchandise market, moreover, it can be used as a hub to access other European markets. It is also evident that trade and investment between Ukraine and European Union are increasing. Similarly, Gosia Hill, Australia's Warsaw-based Senior Trade Commissioner for Central Europe, stated that "Australian business prospects in Ukraine are increasing. We are receiving regular business enquiries from Ukraine through the Austrade office in Warsaw. The sectors of particular interest are: environmental technologies, IT, building, construction and infrastructure as well as commodities, such as coal, steel and timber. Study in Australia is also of interest for children of Ukrainian entrepreneurs" (Cited in Harcourt 2005). In 2005, the growth of the Ukrainian economy was 4.8 percent, which is ahead of Russian Federation on 4.7 percent, while other former Soviet countries are growing at an average of 5.1 percent (Austrade 2005).

Some of the latest achievements in Ukrainian-Australian bilateral relations are the area of technological cooperation. As an example, the recent contract between Australian company Greenwich House and Ukrainian Ukroboronservis according to which Ukraine will

install artillery canons and ammunition on 10 Australian-built patrol vessels (Mission of Ukraine to European Communities 2006). Similarly, Australian military personnel were transported to Iraq on board of AN-124 built by Antonov aircraft factory. There are good prospects for cooperation in sectors of airspace industry, shipbuilding, aircraft construction, and many others.

Nevertheless, the conditions of the business environment in Ukraine remain one of the main obstacles to a greater development of economic cooperation with Australia. Since the early 1990s the Ukrainian government promised to stimulate foreign investment. Section 6 will examine the incentives offered by the Ukrainian government, such as tax (VAT) refund and the provision of support and assistance with the registration and approval procedures (Nikolaiko 2007). The practical application of the incentives, however, will be challenged. This paper will illustrate that in practice the support offered to foreign businesses in Ukraine is minimal.

### 3.2 Macroeconomic performance of the Ukrainian economy

#### 3.2.1 *Crisis-Growth-Crisis*

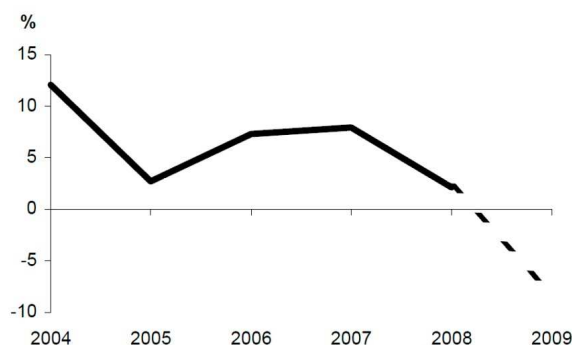
After the contraction of the Ukrainian economy in 1990s, real GDP growth during 2000-07 was strong with an average of 7.5% (DFAT 2009; OECD 2007). However, since 2008 the real GDP growth is declining severely. Real GDP growth during 2004-2009 is illustrated by Table 3.1.

The decline in GDP growth can be explained with the effects of the global economic crisis and the inflation of 25.2%, which is the highest since 1991. Growing dollarisation and the fact that Ukrainian Hryvnia is practically pegged against the US Dollar contributes to inflation volatility and exchange-rate risks. As at July 2009,

Ukrainian Hryvnia is 66% lower than one year ago

and it is clear that financial system remains fragile (UkrSibbank July, 2009).

**Table 3.1: Real GDP growth**



(Source: DFAT 2009)

Prior to the G20 summit, the Australian Prime Minister expressed concerns about deteriorating conditions in Eastern Europe. It was noted that further financial support is needed for the former Eastern Bloc countries (EUAustralia.com 2009). It should be stressed that Ukraine has been hit the hardest as a result of the economic crisis and it is undergoing a

scenario similar to 1997 Asian crisis with major declines in consumer spending and interest rates reaching close to 50%. The political instability is also aggregating in Ukraine.

Ukraine needs very large external financing, otherwise there will be a rise in interest rates, even sharper currency fall, deeper recession and bankruptcies (EFIC 2008). Current account deficit was 7% of the GDP in 2008, which resulted in further deterioration of OECD risk classification of Ukraine from level 5 in 2007 to the maximum level 7 in 2009 (OECD 2009b, 2009a). Two year standby loan from the IMF (US\$16.5billion) is aimed to resolve external funding difficulties, however, by itself it is not sufficient to cover all Ukraine's needs (EFIC 2008). Falling prices and export volumes for metals, which contribute to 40% of Ukrainian exports also indicate deteriorating and risky business environment. It should also be stressed that political instability in Ukraine remains an obstacle to assure future tranches in emergency financing from the IMF. Without the IMF support there is doubt that Ukraine will be able to avoid current balance of payment crisis (Business Monitor International 2009).

The overall growth of the economy during 2000-06 was due to the increased domestic consumption and rising terms of trade. Nevertheless, it is important to underline that during its growth Ukraine experienced relatively low energy prices. Recent as well as possible future sharp increases in price for Russian gas will negatively affect the terms of trade. In the same vein, Ukraine consumed 2.4 times more energy per unit of output than the average across the world (OECD 2007). Therefore, it is clear that unless Ukrainian industry achieves greater energy efficiency any further investment in energy-intensive sectors is at high risk.

Moreover, the report by OECD (2007) indicates that, regardless of the strong economic growth in 2000-2007, Ukraine, similarly to other CIS countries, experiences a significant lag in economic transition in comparison to the Central Europe. Factors that support the economic growth will soon exhaust their potential, and thus, there is a need to advance with market-oriented reforms. That involves regulatory reforms that will address the remaining barriers to enter, exit and compete on the Ukrainian market (OECD 2007). It is identified that the Ukrainian business environment is unfavourable for the increasing level of investment. Businesses face very high legal, regulatory and policy uncertainty, which leads to very high long-term risk.

It should be stressed that political instability is contributing to poor conditions for business operations, it is especially clear with unpredictability of state actions and lack of transparency. Widespread corruption and undermined property rights contribute to high level of risk. It is absolutely essential to improve the quality of public administration as well as



strengthen the rule of law. Inconsistent and conflicting policies give rise to arbitrary bureaucratic action and “rent-seeking”. Inconsistent government policies can be illustrated with the recent attempt to introduce the tax reform that will further stimulate corruption and discriminate against small and medium-sized private businesses. It should be noted that small and medium private firms were one of the main contributors to the economic growth during 2000-2007 period. Ukraine can benefit from deregulation, however, better regulation is necessary rather than simply less regulation in place. It is absolutely essential to close many gaps in legislative and regulatory frameworks (OECD 2007).

There is evidence to claim that higher firm turnover will stimulate greater economic growth; however, in case of Ukraine turnover rates, especially in manufacturing, are extremely low. That again illustrates that there are significant barriers to enter and exit the Ukrainian market. For 1992-2005 period, entering firms in Ukraine are on average 40% more efficient, which is essential to survive in exceptionally difficult business conditions (OECD 2007). New private firms are significantly more efficient than the surviving privatised firms or state owned enterprises. There is also a very weak link between the performance and survival, which can be explained with subsidies provided to specific enterprises. In 2005, around 48% of the Ukrainian capital was still owned by the state or municipal authorities, with only 10-11% in mixed public or private ownership. There is evidence to claim that many SOEs often enjoy informal privileges and at the same time are easy targets for “rent-seeking” by insider managers or well connected outsiders (OECD 2007). State ownership further promotes conflict of interest for the authorities, especially where the role of the state as a regulator conflicts with its role as the owner.

In 2003, the level of product-market regulation for Ukraine was much higher than for any other OECD country, especially in the area of state control, barriers to entrepreneurship, trade and investment (OECD 2007). Overregulation and excessive application of licensing and permits indicate that the barriers to the business growth are much higher than the barriers to enter the market. As an example, the introduction of licensing and quotas for grain exporters in 2006 received strong criticism from the international community. The quota system imposed large losses on grain producers and negatively affected export revenues (Cramon and Raiser 2006). Ukrainian government explains that quota system will ensure that there is enough grain for internal consumption. At the same time, according to UkrAgroConsult oversupply of grain during 2004-07 is much greater than the current export allowance under the quota system. Moreover, the administration of the quota system is highly non-transparent, which again illustrates the magnitude of unforeseen

changes in Ukraine. Taking into account that Ukraine is the sixth largest wheat exporter in the world export restrictions were under major criticism on the international arena. In May 2008, just prior to WTO accession, Ukraine lifted the grain export restrictions (The Office of the United States Trade Representative 2009). This case again demonstrates that the formulation of regulatory policies and the communication with business community is highly unsuccessful.

The abovementioned issues are confirmed by the interviews conducted as part of this paper and illustrate that many obstacles could not be predicted prior to entering the market. The majority of surveyed businesses confirm that excessive rules and regulations are ineffective and add to the time and money spent in course of general business operation. It is clear that regulatory reform that promotes competition will contribute to the stronger economic growth of Ukraine and eliminate some of the major obstacles described above.

Foreign direct investment in Ukraine is far below its potential. The FDI can be supported by the relatively low wages, skilled labour force, access to EU and large CIS markets. The stock of FDI per capita was US\$325 in 2005, which is only 16% if compared to Poland (OECD 2007). Ukraine is missing on substantial positive effect of FDI on its domestic growth due to the weak rule of law, institutional and regulatory problems as well as conflicts of interest within the bureaucracy. According to OECD (2007), privatisation to domestic owners results in lesser productivity growth if comparing to privatisation to foreign owners. While the long term benefits from major foreign privatisation for Ukraine are unclear, privatisation process that ensures greater separation of businesses from the state will ensure increased competition and productivity growth.

### *3.2.2 Accession to the World Trade Organisation*

On 5<sup>th</sup> February 2008, WTO General Council Approved Ukraine's accession to the World Trade Organisation (WTO). The process started with Ukraine's request to participate in General Agreement on Tariffs and Trade in November 2003. It took fourteen years for Ukraine to become a member of WTO. Such a lengthy process can be explained with the fact that Ukraine was a new country with evolving institutions, lack of government experience, unstable legislative and regulatory environment, high level of corruption as well as strong dependence and competition with Russia (Stoler 2009). The main motivation for Ukraine was to access foreign markets, ensure against discrimination on the international arena, protect against Russian influence and allow WTO to guide necessary reforms. It is clear that WTO can be viewed as an external agent that forced numerous governance reforms in Ukraine.

Ukraine underwent a major privatisation campaign, WTO did not aim to put all business into private hands, but to create necessary competition with existing SOEs. Ukraine had to provide reports to WTO Members regarding the developments in the program of privatisation, ensure that the laws and regulations regarding trade and SOEs are in line with WTO requirements. State owned enterprises had to act only based on commercial considerations, overall, non-market economy and price controls had to be abolished (World Trade Organization 2008). However, it is debatable whether the acceptance to the WTO in any way improved the competitiveness of the Ukrainian businesses. Based on the Global Competitiveness Index of World Economic Forum Ukraine fell from the 69<sup>th</sup> position in 2006 to 72<sup>nd</sup> in 2008 (State Agency of Ukraine for Investment and Innovation 2009). A similar tendency is confirmed by the IMD World Competitiveness ranking.

Ukraine changed dramatically as a result of the WTO Bid, which overall improved internal governance and shaped a better environment for foreign businesses. Export subsidies, import substitution subsidies had to be eliminated. In terms of investment, it is no longer required to meet local content requirements, the approval process is simplified and Ukraine can no longer make use of performance requirements (Stoler 2009). While being a member of WTO, Ukraine has to ensure that any regulatory amendments are in line with WTO obligations. Perhaps, recent abolition of 13% import surcharges that were meant to “restore” balance-of-payments is as result of pressures from international actors and other members of the WTO (Global Trade Alert 10 June 2009).

WTO Working Party on the accession of Ukraine aimed to establish a uniform and non-discriminative application of policy and law. In practice, however, it is still a problematic issue, which is confirmed by the interview responses (Refer to Section 6). It should also be noted that loose coupling between formal policies and everyday practices is apparent in Ukraine, which undermines stability and amplifies unforeseen risks.

### **3.3 International rankings and constraints of doing business in Ukraine**

According to the ranking of business practices by the World Bank, Ukraine is ranked 142 out of 183 economies (IFC 2009). One of the main constraints for business operations in Ukraine is the high level of corruption (Refer to Section 6.3.1.4 for the discussion on how corruption affects Australian businesses operating in Ukraine). At least one-quarter of private businesses in Ukraine need to make informal payments to government officials to get things done, especially when dealing with tax officials. There are only four countries in Eastern Europe and Central Asia that have a higher percentage of firms making informal payments: Uzbekistan, Azerbaijan, Kyrgyzstan and Tajikistan (Enterprise Surveys 2009). At the same

time corruption is not uniform across Ukraine. Nearly 87 percent of businesses with foreign participation are expected to give gifts to get construction permits, as opposed to 57 percent of Ukrainian businesses. While giving gifts is more preferred in the Eastern Ukraine, 40 percent of businesses are expected to make informal payments in the Western region (Enterprise Surveys 2009). Power outages were also identified as a concern with an average firm losing over four percent of the sales value.

Most importantly, Ukraine is ranked 181 out of 183 countries for paying taxes (IFC 2009). The lowest ranking can be explained with the high number of payments that are required to be made throughout the year (147 per year), excessive time that is spent on meeting tax requirements (736 hours per year) as well as overall high tax rate (52.2% of profit in 2009). The number of hours spent to meet taxation requirements has decreased from 2085 in 2007 to 736 in 2009, but it remains one of the worst in the world. To date, the Ukrainian government failed to address this issue; it can be stated that the new tax reform will further deteriorate the current situation. (Refer to Section 6 on the discussion of how lengthy tax proceedings affect Australian businesses in Ukraine).

Nonetheless, the business environment in Ukraine is slightly improving, with decreasing levels of corruption, lower average value of collateral required for a loan, and better access to technology. During 2005-2008 the percentage of firms required to make informal payments dropped from 53 to 35 percent, similarly, providing gifts during the meeting also dropped from 51 to 37 percent (Enterprise Surveys 2009; IFC 2009). The value of collateral required declined from 203 percent in 2005 to 136 percent in 2008. Moreover, a centralised registry for charges on movable assets was established and out-of-court enforcement remedies were introduced for secured creditors.

The exporting activity shows a different picture with 8% less exporters in 2008 than 2005. However, the share of foreign inputs rose by at least 5% during the same period. It can be stated that the increase in foreign inputs was a result of improvements in terminal handlings at the Ukrainian ports (IFC 2008). At the same time, the corruption ranking of Ukraine has also deteriorated from 99<sup>th</sup> position in 2006 to 134<sup>th</sup> in 2008 based on the Transparency International index of corruption. Similarly, according to the Index of Economic Freedom of Heritage Foundation the rating of Ukraine has dropped significantly from during 2006-2008. It can be concluded that during the past five years overall business environment in Ukraine weakened if compared to the progress of other countries.

### 3.4 Analysis of trade and investment activities between Australia and Ukraine

In 2008, the trade of goods and services between Australia and Ukraine increased by US\$335,8mil, which is 3.4 times higher if compared to 2007. Goods turnover remains dominant (98.8%), with exports of US\$412,8mil and imports of US\$60,6mil (UN Commodity Trade Database 2009). Intensified trade can be explained with the increase in exports to Ukraine from US\$122.5mil in 2007 to US\$290.3mil in 2008. Table 3.2 provides the summary of trade of goods and services for 2004-2008.

**Table 3.2: Trade of goods and services between Australia and Ukraine  
(2004-2008)**

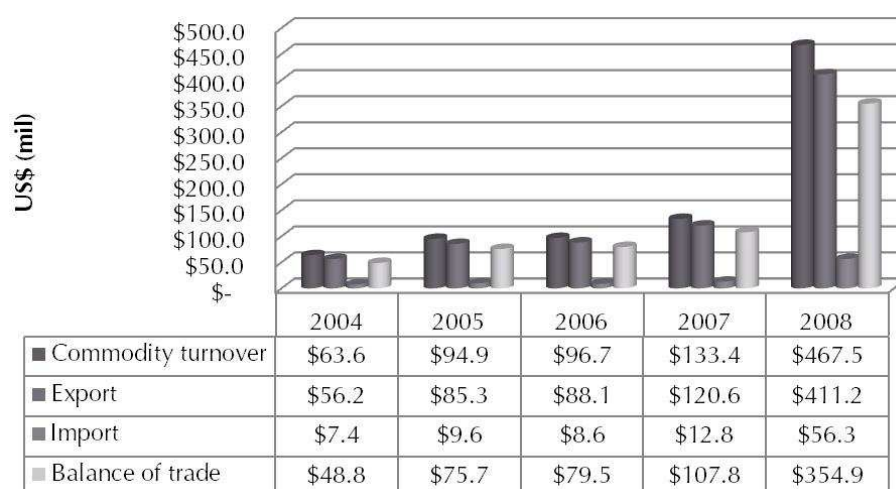
	2004	2005	2006	2007	2008	Increased or decreased (2007-2008)	
						(US\$ mil)	(%)
Trade of goods and services - total	65,1	96,8	99,8	137,6	473,4	335,8	344,0
- goods	63,6	94,9	96,7	133,4	467,5	334,1	350,4
- services	1,5	1,9	3,1	4,2	5,9	1,7	140,5
Export – total	57,1	86,3	89,5	122,5	412,8	290,3	337,0
- goods	56,2	85,3	88,1	120,6	411,2	290,6	341,0
- services	0,9	1,0	1,4	1,9	1,6	-0,3	84,2
Import – total	8,0	10,5	10,3	15,1	60,6	45,5	401,3
- goods	7,4	9,6	8,6	12,8	56,3	43,5	439,8
- services	0,6	0,9	1,7	2,3	4,3	2,0	187,0
Balance of trade - total	49,1	75,8	79,2	07,4	352,2	244,8	327,9
- goods	48,8	75,7	79,5	107,8	354,9	247,1	329,2
- services	0,3	0,1	-0,3	-0,4	-2,7	-2,3	675,0

(Source: Ministry of Economics of Ukraine 2009)

#### 3.4.1 Commodity turnover during 2004-2008

Overall, trade relations between Australia and Ukraine remain minimal. However, since 2004 commodity turnover has increased by US\$403.9mil (7.4 times), which is illustrated by Table 3.3.

**Table 3.3: Commodities turnover between Australia and Ukraine (2004-2008)**



During 2004-2008 Australian exports increased by US\$403.9mil and contributed to 88% of overall commodity trade. It should also be noted that Australia maintained a strong positive balance of trade with Ukraine.

The main exported commodities to Ukraine in 2008 were:

- Mineral resources – US\$372.4mil (90.6%), that includes:
  - Manganese ore –US\$306.6mil (74.6%),
  - Aluminium ore – US\$37.4mil (9.1%),
  - Coal – US\$28.4mil (6.9%);
- Transport vehicles – US\$18.2mil (4.4%);
- Precious metals – US\$3.9mil (1.0%), including:
  - Coins – US\$3.8mil (0.9%);
- Machinery, equipment and parts thereof – US\$3.8mil (0.9%);
- Misc. industrial products – US\$3.5mil (0.9%);
- Chemical products – US\$3.5mil (0.9%), including:
  - Medicine – US\$1.1mil (0.3%)
- Instruments and apparatus – US\$1.6mil (0.4%);
- Meat and edible meat offal – US\$1.4mil (0.3%).

(Source: Ministry of Economics of Ukraine 2009; UN Commodity Trade Database 2009; State Statistics Committee of Ukraine 2009b; ABS 2009)

The main imported commodities from Ukraine in 2008 were:

- Metal and steel – US\$26.5mil (47.0%);
- Fertilizers – US\$16.2mil (28.7%);

- Machinery, equipment and parts thereof – US\$7.9mil (14.0%);
- Silver – US\$1.5mil (2.9%);
- Yachts – US\$0.9mil (1.5%).

If compared to 2007, there is an increase in the imports of the abovementioned commodities, however, due to relatively small economic activities between Australia and Ukraine such progress cannot be regarded as significant or consistent.

Significant increase in exports to Ukraine during 2007-2008 is driven by the increases in the supplies of the following commodities:

- Manganese ore by US\$246.2mil (5.1times);
- Coal by US\$28.1mil (no supplies in 2007);
- Transport vehicles by US\$13.3mil (3.7 times);
- Coins by US\$3.8mil (no supplies in 2007);
- Meat and edible meat offal by US\$1.4mil (no supplies in 2007)

At the same time, export of aluminium ore decreased by US\$8.4mil, which is around 18% less than the exports in 2007.

#### *3.4.2 Trade in services during 2008*

The main imported services from Ukraine during 2008 were:

- Transportation services – US\$2.2mil (51.4%);
- Travel – US\$0.9mil (20.3%);
- Computer services – US\$0.8mil (19.3%);
- Research services – US\$0.2mil (4.8%).

Services that Australia exported to Ukraine in 2008 are as follows:

- Legal services and market research – US\$0.6mil (38.5%);
- Government services that are not included in any other category – US\$0.5mil (32.8%)
- Travel – US\$0.2mil (12%).

#### *3.4.3 Commodity turnover during 2008-2009*

As expected, due to the overall trade turnover being minimal, regardless of the recent 340% increase, both exports and imports to Ukraine dropped significantly during January – August 2009. Based on the information provided by the Ministry of Economics of Ukraine (2009), commodity turnover has dropped by 3.8 times, comparing to consecutive

period in 2008. The underlying reason is the fall in exports from Australia by US\$210.5mil (370%). This has had a significant effect, because in 2008 Australian exports contributed to 88% of the overall turnover. Moreover, from the beginning of 2009 Australia also imports 4.3 times less products from Ukraine, which at the moment is as low as US\$10.3mil. Table 2 illustrates the recent regress in trade between Australia and Ukraine.

**Table 3.4: Commodities turnover between Australia and Ukraine  
(Jan-Aug 2008/2009)**

	Jan – Aug 2008	Jan – Aug 2009	Increase/Decrease	
			( +/- )	(%)
Commodity turnover	331,8	87,2	-244,6	380
Export	287,4	76,9	-210,5	370
Import	44,4	10,3	-34,1	430
Balance of Trade	243,0	66,6	176,4	360

(Source: State Statistics Committee of Ukraine 2009a)

The main exported commodities to Ukraine in 2009 are:

- Manganese ore – US\$61.6mil (80.0%);
- Aluminium ore – US\$4.9mil (6.3%);
- Vehicles – US\$2.9mil (3.8%);
- Machinery, equipment and parts thereof – US\$1.2mil (1.6%);
- Silver – US\$1.6mil (1.5%)

The main imported commodities from Ukraine in 2009 are:

- Machinery, equipment and parts thereof – US\$5.8mil (56%);
- Fertilizers – US\$2.7mil (26.7%);
- Transport vehicles – US\$1.3mil (12.4%).

Therefore, the drop in Australian exports during January – August 2009 occurred in the following categories:

- Manganese ore – by US\$189.0mil (4.1 times);
- Aluminium ore – by US\$13mil (3.7 times);
- Transport vehicles – by US\$4.9mil (3.7 times);
- Misc. industrial products – by US\$3.0mil (only US\$73,000 during 2009);
- Silver – by US\$8.0mil.

The decrease in Ukrainian imports during 2009 can be seen in the following commodities:

- Metal and steel – by US\$28mil (only US\$135,000 during Jan-Aug/2009);



- Fertilizers – by US\$9.9mil (4.6 times);
- Silver – by US\$0.7mil (only US\$2,000 during Jan-Aug/2009)

Any increases in imports of other commodities from Ukraine remain minimal (Ministry of Economics of Ukraine 2009; UN Commodity Trade Database 2009; State Statistics Committee of Ukraine 2009b).

#### *3.4.4 Trade in services during 2009*

Services imported from Ukraine during January – August 2009:

- Computer services – US\$0.7mil (41.4%);
- Transportation services – US\$0.4mil (20.7%);
- Research services – US\$0.3mil (16.0%);
- Travel – US\$0.2mil (9.8%).

Services exported to Ukraine during January – August 2009:

- Various professional, business and technical services – US\$0.9mil (75.5%);
- Government services that are not included in any other category – US\$0.3mil (21.0%)

(Source: Ministry of Economics of Ukraine 2009)

It can be seen that trade in services between Australia and Ukraine is close to nothing. However, based on the research conducted, there is a much greater potential for further cooperation in the provision of services between the two countries. This issue will be addressed in greater detail in Analysis of results part of the paper.

#### *3.4.5 Investment cooperation*

By July 2009, Australia overall invested US\$7.4mil into 20 Ukrainian companies (Ministry of Economics of Ukraine 2009).

Direct investments from Australia were made in the following categories:

- Industry – US\$4.7mil (63.8%) – prior to 2009;
- Transport vehicles trade – US\$1.6mil (21.7%);
- Engineering and various company services – US\$0.6mil (8.3%).

Based on the information provided by the State Statistics Committee of Ukraine, no direct investment was made into Australian economy as at July 2009.

## **4. RESEARCH DESIGN AND METHODOLOGY**

### **4.1 Qualitative Method**

It should be noted that the literature on the subject of business activities between Australia and Ukraine is very sparse. Academic journals in the area of international business seem to neglect the significance of the Eastern-European context. The only empirical studies, to the extent of my knowledge, are surveys and reports conducted by the International Finance corporation and the Organisation for Economic Co-operation and Development (Refer to Section 3 and Section 6, Section 6.3.1.3 for the detailed discussion of the reports). At the same time there is no empirical evidence presenting the perspective of the Australian companies operating in Ukraine. Therefore, qualitative approach was selected as the research strategy for the investigation.

As argued by Silverman (1993) there are no concrete grounds that determine whether qualitative or quantitative research should be used and it all depends on the initial purpose of the project. Rather than engaging in the discussion of the benefits and shortcomings of qualitative and quantitative methodologies, it will be argued that qualitative method has the highest potential for answering the research question. As outlined by Strauss and Corbin (1990) qualitative methods can be used to explain a phenomenon that little is known about and it is necessary to build new theories as well as test existing data. Therefore, a qualitative approach is appropriate for this study as there is very little known about the obstacles that Australian companies face when operating in Ukraine.

By employing qualitative methodology this study will be looking for patterns and interrelationships between various barriers that Australian companies experience in Ukraine. Furthermore, due to limited research in this area it is yet difficult to measure the degree of specific characteristics of the Ukrainian business environment. Hence, this study will observe and analyse the main factors that undermine further economic development between Australia and Ukraine (Kirk and Miller 1986). The goal of this paper is to establish a set of features of Ukrainian and Australian business environments and examine its influence on the economic relations between the two countries.

### **4.2 Grounded Theory**

Grounded theory is defined as an “inductive theory discovery methodology that allows the researcher to develop a theoretical account of the general features of the topic while simultaneously grounding the account in empirical observations of data” (Martin and Turner 1986). In line with the characteristics of the Grounded Theory presented by Charmaz

(2001), in this study the researcher was closely involved in the collection and analysis of the data, categories and codes were created based on the data collected rather than from preconceived hypothesis. Therefore, the behaviour of the process that influence economic cooperation between Australia and Ukraine is explained.

Applying systematic coding processes in this study prevents speculative and unfounded assumptions, guards against preconceived ideas and biases as well as ensures rigour and relevance (Fernández and Lehmann 2005; Glaser 1998; Sarker, Lau, and Sahay 2001; Strauss and Corbin 1990; Urquhart 2001). At the same time, pre-existing research was taken into account to allow a better approach in processing the large amount of data (Glaser 1998). Grounded theory will assist in providing the conceptual gap to knowledgeable people in the area and further contribute to their understanding of the research context (Glaser 1998). Qualitative data coding tools (NVivo) were widely used in the analysis of data. That allowed to ensure high quality of coding as well as to compare incidents across the whole sample.

#### *4.2.1 Empirical data collection*

In-depth interviews were considered as the most appropriate qualitative technique for this study. To address the research context, personal interviews were conducted with owners, managing directors and top-level managers as well as individuals that are closely involved in the discussion of business activities between Australia and Ukraine (Refer to Section 5 for sample description). The length of the interviews ranged from 30 to 120 minutes. Interviews were semi-constructed, which allowed greater adaptability and flexibility of the discussion. Ukrainian participants were addressed in English, Ukrainian or Russian, depending on the preferred language of communication by the participant. The general structure of the interview was controlled by the question guidelines (refer to Appendix 1).

## **5. SAMPLE DESCRIPTION**

### **5.1 Sample Details**

Nine companies from a broad range of industries participated in this study. Seven out of nine companies in the sample have onshore operations in Australia and only two are operating in Ukraine. Moreover, as part of this research interviews were conducted with people who facilitate discussions between business parties and thus are closely involved in current business activities between Australia and Ukraine. The characteristics of the companies vary and therefore it is likely that the barriers for trade and investment identified by the respondents will differ. In this section the description of case firms and other respondents is presented.

Table 5.1 presents the summary of the companies who participated in this study.

**Table 5.1: Features of the sample companies**

	<b>Company Name</b>	<b>Informants position</b>	<b>Initiated</b>	<b>Entry mode</b>	<b>Outcome</b>
Australia	ABB Grain Ltd.	Managing Director; Business Dev. Manager	2007	Joint Venture	Positive
	OilExplore	Managing Director	1995	Joint Venture	Negative
	WoolStock	Closely involved in neg.	1995	-	Negative
	DniproIndustrial	Owner	1998	-	Negative
	EuroBeverages	Owner	2005	Importing	Positive
	SoftwareEng	Owner	2002	No Presence	Positive
	MedTech	Owner	2007	No Presence	Positive
Ukraine	UkrBeer	Export Manager	2005	Exporting	Positive
	UkrSpirit	Export Manager	2005	Exporting	Positive

Note: \* Permission was obtained from ABB Grain Ltd. to use real company name for the purposes of this research. Other company names are not genuine, however, identify the area of the company's activities.

The majority of informants who are involved in business negotiations between Australia and Ukraine are either owners or top-level managers. The only case that is different is WoolStock Company, the informant refused to lead negotiations with Ukraine, however, closely followed the discussions on the issue. Export managers were interviewed for both of the Ukrainian companies who are in charge of any dealings with distributors from Australia and other countries.

The sample contains companies that conducted negotiations on offshore activities on different dates. Nevertheless, it will be illustrated that the issues that the Australian companies had are relatively similar during the past 20 years. Both of the Ukrainian companies, however, started exporting its products to Australia in 2005. It should be noted that one of the Australian distributors, who works together with both of the Ukrainian companies, is also included in the sample. The companies were randomly selected; it was attempted to provide maximum variation to ensure that the sample represents the full context of the research issue.

It was expected that ABB Grain Ltd. and OilExplore would outline a greater variety of obstacles that were faced while trying to establish offshore operations in Ukraine. That can be explained with the fact that the level of involvement of these businesses was much broader. Also, the time spent in negotiations by the two companies is over 2 years. The choice of the entry mode will determine the level of involvement in Ukraine and thus influence the number risks that the company is exposed to.

It should be stressed that all Australian participants who were leading the formation of offshore operations in Ukraine had significant background about Eastern Europe and

Ukraine in particular. It is clear that having considerable knowledge as well as connection to Ukraine is one of the preconditions for an attempt to build a bridge in economic relations between the two countries. At the same time, it cannot be claimed that the Ukrainian background in any way determined the success of the initial project.

In case of Ukraine, industry experience does not directly influence the success of the internationalisation attempt. As an example, ABB Grain Ltd. and OilExplore are both highly competitive and experienced actors. Nevertheless, regardless of significant obstacles to business operations, ABB Grain was able to successfully establish a joint venture in Ukraine, whereas, OilExplore after 3 years of negotiations could not proceed with the project.

## **5.2 Company Reports**

### *5.2.1 Australian businesses*

#### **ABB Grain Ltd.**

This company is Australia's premier and largest agribusiness, with A\$1.6 billion market capitalization. It is a key grain supplier to domestic and international processors, with export markets in more than 40 countries. It is Australia's largest barley marketer, also, biggest maltster and significant global producer. The revenue for 2008 was A\$2.2 billion, continued growth and diversification is the result of the strategy highlighted by expansion into Ukraine and New Zealand. ABB Grain Ltd. Employs approximate 1,200 staff across Australia, New Zealand, China and Ukraine.

In August 2007, ABB Grain Ltd. entered into a joint venture with Groupe Soufflet (one of the world's largest malting businesses), establishing a company called New World Grain. New World Grain now employs more than 45 staff in Ukraine and has offices and representatives in Kyiv, Mykolaiv, Kirovograd, Poltava and Crimea. ABB Grain along with joint venture partner Groupe Soufflet see great potential in Ukraine.

#### **OilExplore**

OilExplore is an American company which is highly competitive on the international level. It has operations and offices in Australia and many other foreign countries. The Managing Director at the time is the Australian citizen and was in charge of all the dealings regarding the expansion to Ukraine. This person is highly experienced in oil exploration and production. Successful contracts were signed with Australia, Middle East, Denmark, offshore Egypt and other countries.

The project involved developing an oil field that Ukraine could not proceed with due to financial and technological limitations. Negotiations on the project were held for 3 years,

during 1995-1998. From the perspective of OilExplore it would have been one of the easiest projects the company has ever developed. Unfortunately, due to high level of risk and fairly unstable environment OilExplore was unable to proceed with the project.

#### WoolStock

During 1995-96 Australia had an overstock of wool, which could have been processed at the Ukrainian textile mill. The technology that Ukraine had at the time was capable of processing the quantity required by the Australian side. Nevertheless, the textile mill had no modern technology and computers, which would have been provided by Australia. Ukraine would receive necessary technology for the price of \$20 million as well as half of the unprocessed wool stock. The price of unprocessed wool is very low, however, if it is processed the price is close to A\$50 million dollars. Ukraine at the same time would gain access to Western European markets.

#### DniproIndustrial

In 1998, the business attempted to cooperate with a Ukrainian company in the area of space science. The size of the business is small, however, at the time the company already had dealings with the Russian Federation. Business owner is originally from one of the former Soviet states and has had experience of dealings in Eastern Europe. Negotiations with the Ukrainian company were lengthy and unsuccessful.

#### EuroBeverages

This company is the distributor of alcoholic beverages, with operations in Poland, Czech Republic, Ukraine and other Eastern-European countries. EuroBeverages is one of the largest distributors of European alcoholic beverages into Australia and the United States. The company is well experienced in logistics and distribution of various products for the last 10 years. The owner of the company is originally from Eastern Europe and has excellent knowledge of Eastern-European business culture. Current business with Ukraine is profitable, however, if other business opportunities emerge EuroBeverages will reconsider the prospects of current dealings with Ukraine.

#### SoftwareEng

The company developed ATM simulation program for the Australian banks. The purpose of the software is to predict how many notes and of what value will be withdrawn from the ATM on the specific date. The company employed Ukrainian graduates in mathematics, physics and IT to work on the development of the system. It should be noted that SoftwareEng has no physical presence in Ukraine to avoid bureaucracy problems and internal instability. The owner of the business started the project as a result of previous

dealings with Ukraine that were unsuccessful. However, networks and contacts from the first project were used to establish current business cooperation.

#### MedTech

The business structure of MedTech is similar to SoftwareEng as both of the companies do not have the physical presence in Ukraine. MedTech is employing Ukrainian graduate and senior doctors who undergo training and then assist in using specific medical equipment. Similar to all Australian companies that had dealings with Ukraine, the owner of MedTech has close ties with Ukraine and was closely involved in at least two other projects in Ukraine.

#### 5.2.2 *Ukrainian businesses*

##### UkrBeer

The share of the company in Exports of Ukrainian beer in 2008 was over 75%. This is one of the first companies from the former Soviet Union to begin exporting beer abroad. The company exports to over 33 countries of the world. The export volume in 2008 was increased by 11.4%. UkrBeer started exporting to Australia in 2005. The initiator of exporting to Australia was EuroBeverages. UkrBeer has very minor barriers exporting to Australia, all distribution and licensing of products is taken by EuroBeverages. However, taking into account long geographic distance between Australia and Ukraine the market for UkrBeer products in Australia is relatively small.

##### UkrSpirit

This company exports alcohol beverages to Australia with marketing operations being very similar to UkrBeer. One of the distributors of UkrSpirit in Australia is also EuroBeverages. Similarly, there are no strong barriers for exporting its product to Australia. Nevertheless, high import tax on alcoholic beverages in Australia forces the company to remain highly efficient and competitive. Unlike UkrBeer, the market for UkrSpirit products in Australia is expected to grow.

### 5.3 **Other Informants**

To ensure that the sample used in this research has the best chance of truly representing the context of the research question, three individuals were interviewed that are closely involved in discussions on building stronger economic and political ties between Australia and Ukraine. The informants take part in meetings of Australian and Ukrainian parliamentary delegations. They aim to stimulate further negotiations between businesses as

well as provide necessary assistance in overcoming the barriers to economic cooperation between Australia and Ukraine.

## **6. ANALYSIS OF FINDINGS AND DISCUSSION**

This section provides analysis and summaries of the findings. The paper discusses the three main themes: First, the benefits of further economic cooperation between Australia and Ukraine; second, the role of barriers and obstacles to a greater economic cooperation between the two countries, and third, recommendations will be provided on how to overcome current obstacles and stimulate further development of economic ties between Australia and Ukraine.

### **6.1 Across Sample Analysis - Summary**

This study is using qualitative methods to analyse the interview data. Comparisons were undertaken to outline similarities and differences across the positions expressed in relevance to the research questions. Finally, the following categories and themes illustrate the main barriers to bilateral business relations with Ukraine:

- 1.) Unstable and volatile business environment:
  - a. Macroeconomic performance
  - b. Political instability
  - c. Regulation and policy problems:
    - i. Overregulation
    - ii. Tax
  - d. Weak rule of law – Corruption
- 2.) Culture: Work ethic
- 3.) Difficult to deal and negotiate

The relationship between each category and subcategory is identified in Table 6.1 below.



**Table 6.1: Main Themes Emerging From the Interviews - Ukraine**

Barriers and Obstacles - Ukraine										
	Unstable and volatile environment:	» macroeconomic performance	» political instability	» regulation and policy: overregulation	» regulation and policy: tax	» weak rule of law: corruption	Culture: Work ethic	Difficult to deal and negotiate	Geographic distance	Image on the international arena
ABB Grain Ltd.	+	+	+	+	+	+	+	+	+	+
OilExplore	+		+	+	+	+		+		
WoolStock	+		+	+		+	+	+		+
DniproIndustrial	+	+	+	+		+		+		
EuroBeverages	+		+			+	+	+	+	+
SoftwareEng	+		+	+	+	+				
MedTech	+		+	+	+	+			+	
UkrSpirit	+		+	+	+	+			+	
Informant #1	+		+	+	+	+		+		+
Informant #2	+		+							
Informant #3	+	+							+	

While there are only two Ukrainian companies that participated in this study, it is clear that the Australian business environment poses significantly less obstacles for further development of economic ties with Ukraine. In the same vein, the majority of businesses identify no significant obstacles in Australia that would undermine bilateral relations with Ukraine. It is necessary to take into account that all companies that claim obstacles of the business environment being insignificant are established in Australia. Thus they are likely to underestimate the difficulties that Ukrainian business face when expanding to Australia.

The main issues are categorised as follows:

- 1.) Minimal interest of Australia in Ukraine
- 2.) Unwillingness to accept offshore risks
- 3.) Funding problems, if dealing with Ukraine
- 4.) Low demand due to small market size
- 5.) Geographic distance
- 6.) High level of tax on specific products

Table 6.2 below presents the summary of the main factors that interviewees identified as barriers in Australia.

**Table 6.2: Main Themes Emerging From the Interviews - Australia**

Barriers and Obstacles - Australia						
	Minimal interest in Ukraine	Unwillingness to accept offshore risks	Funding (only if dealing with Ukraine)	Demand, market size	Geographic distance	High level of tax (specific products)
ABB Grain Ltd.		+	+	+		
WoolStock		+				
MedTech					+	
UkrSpirit				+	+	+
UkrBeer					+	
Informant #1	+	+				
Informant #2	+					
OilExplore	insignificant					
DniproIndustrial	insignificant					
EuroBeverages	insignificant					
SoftwareEng	insignificant					
Informant #3	insignificant					

## 6.2 Potential for a greater economic cooperation between Australia and Ukraine

A general discussion of benefits of economic cooperation between the two countries is introduced in Section 3. This section, however, will analyse the potential for greater economic cooperation in light of the views expressed by the participants of the study.

### 6.2.1 Benefits for Australia

The vast majority of the participants identify significant potential for a greater cooperation with Ukraine. It is only EuroBeverages that doubt whether there are any significant benefits and claim that if better opportunities emerge it is likely that they will reconsider current dealings with the Ukrainian suppliers. This position can be explained with the fact the EuroBeverages is not strongly dependent on the products imported from Ukraine, as other Eastern European countries are highly competitive in the same business sector. Other businesses, on the other hand, conduct dealings with Ukraine in the areas that allow them to achieve greater competitive advantage.

It is outlined that the business environment in Ukraine has developed significantly to support business developments, if compared to early 1990s. While there are some remains of

the old system, the economy in Ukraine allows consumers to choose whether or not they are likely to support “old system” businesses.

**“So you have look at “Arena” and you say to yourself how does this thing operate? Who in effect funds that? The lease is expensive, it’s not profitable... is this an example of more like the old system which perhaps could operate more efficiently and at the moment it doesn’t because it’s targeting a certain group of people ...rather than addressing everybody?**

**Now I’m not sure that there’s too much western investment in that; there seems to be a lot of Ukrainian investment”** (Informant #1, personal communication, 11th September 2009)

This evidence supports the argument raised by the OECD report (2007), which states that regulatory and competition reforms in Ukraine are critical for further economic development. It is illustrated that the Ukrainian government often provides informal support to some of the businesses and thus there is a very weak link between the performance and survival (Refer to Section 3 for more detail).

The potential in Ukraine is not concentrated in Kyiv only. While it is one of the most developed cities in Ukraine, other regions have different specialisations and thus should not be neglected. As an example, MedTech, SoftwareEng and ABB Grain Ltd all operate in different regions of Ukraine. That again illustrates the potential for a broad range of Australian businesses in Ukraine.

Ukraine has a highly educated workforce that is much cheaper than elsewhere in the world. OilExplore identified that the education of Ukrainian geologists is comparable at the international level. Similar views are also expressed by MedTech and SoftwareEng.

**“Cheap, very competitive labour, high level of English language, mathematical skills are superior. Best educated people in the field of math, physics and IT”** (SoftwareEng, personal communication, 8th October 2009)

In fact Australia and Ukraine are very similar, however, the position that the competitiveness might work against the cooperation between the countries should not be taken. This view is also supported by the ABB Grain Ltd (ABB Grain, personal communication, 14<sup>th</sup> October, 2009).

Nevertheless, by expanding to Ukraine ABB Grain Ltd. gained access to a market that is much larger than in Australia.

**“...Ukraine attracted us for two reasons. The first reason was they produce around 40 or 50 million tonnes of grain, per annum. They have a domestic requirement of around 35 million ... and they export the surplus. So that’s not dissimilar to Australia.**

**The big thing is that Ukraine's production yield is about 50% of Western Europe. There is a potential to double the amount of grain produced, which would make it a super power exporter."** (ABB Grain Ltd., personal communication, 14th October, 2009).

There is a reasonable potential for Australian businesses to conduct commerce with Ukraine, **"particularly after Ukraine gets over its current economic difficulties ... Pre-Global financial crisis, it was taking active steps to open up its borders and improve its investment climate. It is highlighted by the fact it joined the WTO ... and is in discussions with EU regarding the free trade agreement"** (Informant #3, personal communication, 11<sup>th</sup> September 2009). [The role of WTO accession is discussed in Section 3] There are constant discussions on business perspectives between the two countries:

**"They have been working in things like for example rocketry, ... all those sorts of armed forces and military. They have been having some serious conversations"** (Informant #1, personal communication, 11th September 2009)

However, it is necessary to provide greater incentives and support to stimulate the development of bilateral relations.

**"Australia has a high interest in Ukraine, but also the high level of risk, that is related to the character of the government politics, and alarms the potential investors. Any benefits that are associated with the potential in Ukraine are outweighed by the lack of transparency as well as very limited government guarantees for the investors"** (Translated from Ukrainian, UkrSpirit, personal communication, 5th November, 2009)

All of the companies agree that the level of risk is very high. Furthermore, it is crucial not to underestimate this factor prior to the establishment of business dealings with Ukraine. **"It is a great opportunity but there are all these other hidden rules that you've got to learn to play by and unless you play by those rules you just don't play"** (Informant # 1, personal communication, 11<sup>th</sup> September 2009). Similar position is also held by the ABB Grain Ltd.

#### *6.2.2 Benefits for Ukraine*

Australia can share its experience and technologies with Ukraine. While Ukraine and Australia specialise in similar industries, the level of the development is different and thus motivates closer bilateral ties. The farm system in Ukraine can be significantly improved by using the structure recommended by the ABB Grain Ltd. It is important to make farmers more efficient in Ukraine. Ukraine can become very powerful in agriculture and grain exports in particular. It is necessary to promote cooperation between farmers and develop a single desk where the farmers receive the same amount of money for the first and the last tone of

grain (ABB Grain Ltd., personal communication, 14<sup>th</sup> October 2009). That is similar to the strategy used in Russian Federation, where farmers act collectively rather than compete, decrease the price and thus limit the benefits of greater exports.

Furthermore, the benefit for Ukraine can be illustrated by looking at the negotiations between OilExplore and Ukrnafta. The potential revenue to Ukraine, if the negotiations were successful, would have been over US\$1billion. The value of the investment by OilExplore could have been over US\$400million. Unfortunately, regardless of the interest and incentive by OilExplore, the project was unsuccessful and the potential benefits were not realised. Nevertheless, at the time of negotiations Ukraine received US\$7 million investment from OilExplore. The money went into reconstruction of the premises and buildings, provision of technology, education and other purposes. All work was conducted by the Ukrainian labour, moreover, over 30 Ukrainian geologists received access and education to the latest technology that was not present in Ukraine at the time. Geological office was formed in L'viv, Ukraine. The initial project would have created new jobs, infrastructure and further the technology transfer.

On 3<sup>rd</sup> July 1998, as a result of negotiations between OilExplore and Ukrnafta, the first International Gas Conference was held in L'viv. The standard of the presented material at the Conference was equal or better than the work done in Houston, the United States of America. It should be stressed that all the materials were prepared by the Ukrainian geologists and the only assistance that they received from OilExplore was modern technology that was used for the presentational purposes. If the outcome of the negotiations was successful, in the long run, Ukraine could buy out the shares of OilExplore (OilExplore, personal communication, 12<sup>th</sup> October 2009).

Ukrnafta would receive 51% of profits, where as OilExplore agreed to the share of 49%. All the capital would have been provided by OilExplore, with an interest on the loan of 1.5%. The interest was very low and Ukrnafta would have to repay the loan by contributing 40% of its profits each year that are earned from the project. Even so, the project received a strong opposition that was politically motivated and as a result the outcome of the negotiations was unsuccessful.

The vast majority of the interviewees argue that any type of business cooperation between Australia and Ukraine is beneficial. Foreign businesses are bringing in income and stimulate further development and growth of the Ukrainian economy.

### **6.3 Barriers and risks of the business environment in Ukraine will outweigh any benefits?**

#### *6.3.1 Highly unstable and volatile environment*

The risks that foreign businesses face while operating in Ukraine are excessive, it is not uncommon for the Australian companies to state “there is just too much risk, no matter how good the future is”. The risks in Ukraine are often underestimated, which is also the case for the majority of the companies included in this study. As outlined in Table 3.1, all of the participants characterized Ukrainian business environment as highly unstable and volatile. The conditions of the business environment in Ukraine are constantly changing, which makes it practically impossible for the businesses to estimate the risks of business operations (ABB Grain Ltd., personal communication, 14<sup>th</sup> October 2009).

**“The proposals are on the table, people discuss and people then ultimately say, ‘Okay now what are the guarantees?’. Confidence, you’ve got to have confidence in the system”**

**“Everybody wants to have access but I think the point that you made before is that you want to play within the rules. And providing you know the rules then you can play. Trouble is that the rules keep shifting. And that’s the biggest problem ...”** (Informant #1, personal communication, 11<sup>th</sup> September 2009).

The significance of unstable conditions in Ukraine will be illustrated by assessing the following issues: macroeconomic performance, political instability, regulation and policy problems: overregulation and tax, as well as weak rule of law that is conditioned by the high level of corruption (Refer to Table 3.1 for the summary of the risks businesses face while operating in Ukraine).

##### *6.3.1.1 Macroeconomic performance*

The poor microeconomic performance of Ukraine during the financial crisis strongly undermined attractiveness of Ukraine for foreign investment. The rating of business risk in Ukraine according to OECD is currently at its maximum level 7. That in fact will influence the price of short-term and long-term credit insurance for the Australian businesses that are dealing with Ukraine. Finance providers reflect on **“large concerns about the country’s ability to service its external debt”** (Informant #3, personal communication, 11<sup>th</sup> September 2009). As a result of deteriorating economic performance ABB Grain Ltd. and other businesses in Australia found it difficult to obtain funding while dealing with Ukraine.

The implication of the global financial crisis on Eastern Europe and Ukraine in particular are discussed in Section 3.

#### *6.3.1.1.1 Exchange rate*

Over the past year, ABB Grain Ltd. suffered significant losses as a result of the sudden drop in the value of Ukrainian Hryvnia. As already discussed in Section 3, as at July 2009, the value Ukrainian Hryvnia is 66% lower than one year ago and remains highly fragile. The fact that VAT (equivalent of Australian GST) is paid in US Dollars and the refund from the Ukrainian government is received in Hryvnias, any exchange rate fluctuations will directly affect profit values. Hedging against exchange rate volatility is problematic due to relatively small liquidity in the Ukrainian market (ABB Grain Ltd., personal communication, 14th October 2009).

#### *6.3.1.1.2 Funding*

Businesses also found it difficult to obtain funding in local currency, to hedge against the fluctuations of the currency exchange rate. The liquidity of the Ukrainian market is small and it is lengthy to sign an agreement with a local bank. Moreover, the interest is also significantly higher than in other countries. ABB Grain Ltd. presented arguments that illustrate the lack of liquidity as well as the difficulty of signing an agreement with a local Ukrainian bank.

While the issue of macroeconomic performance is significant, **“main obstacle is to a great extent political instability, economic instability to a lesser degree”** (DniproIndustrial, personal communication, 25<sup>th</sup> August 2009). The evidence for this argument is presented in the next section.

#### *6.3.1.2 Political instability*

As already discussed in Section 3.2.1, the potential for greater economic activity between Australia and Ukraine is high. In spite of this, the vast majority of interviewees identified current political instability in Ukraine as one of the major obstacles. It is clear that businesses have to go through **“so many problems to harvest these seeds and to make them grow. Providing that you have the right wheel in the government progress is potential. But right now the government undermines any improvements and maintain the strongest control over businesses”** (MedTech, personal communication, 8<sup>th</sup> October 2009).

DniproIndustrial also supports this argument and stated that **“the triangle of power struggle currently existing has to be broken to achieve any improvement. Old Soviet apparatchiks are at power, holding the main positions...”** (Personal communication, 25th August 2009).

It is cannot be stated that the political situation in Ukraine has had any significant improvement since late 1990s. The main concern that WoolStock had in 1995 is identical to the views expressed by those currently involved in business with Ukraine. The quote below illustrates the significance of this issue.

**“A lot of pessimism at that time about the future, whether it will revert back to communism, whether private enterprise will take off, will there be dictatorship... Will we get our money back – political risk. Effectively it is political risk that the people are looking at”** (WoolStock, personal communication, 11th September 2009).

In the same vein, political instability within the country can be the answer for the unsuccessful outcome of negotiations between Ukrnafta and OilExplore in 1995-1998.

**“...politically motivated, emotional problem, resulted in extensive campaigning against the project. Bureaucracy is a problem, people were blocking the project, those were politicians, not the technicians. It took nearly 1 year to sign the license”** (OilExplore, personal communication, 12<sup>th</sup> October 2009).

The difficulty of dealing with the Ukrainian government and the fact that it is often a significant interruption to the Australian businesses should not be underrated. It can be difficult to comprehend, how government instability affects the business activity. The relevance of this argument is explained below:

**“One of the biggest problems with Ukraine is dealing with government. It’s a joke because until you establish I suppose what we have similar to here ... a system which has two houses, which has government, which has an opposition rather than having party lists ... people don’t even know who has been elected. ...they jump from party to party. Now, do you want people to do business with that sort of government? Had he [referring to Viktor Yushchenko, current president of Ukraine] been stronger in terms of corruption I think you would have had a completely different Ukraine today in terms of confidence.**

**...Who are you [referring to Ukrainian politicians] accountable to? ... You’re accountable to nobody. They can’t touch you...**

**You want a strong Ukraine, constitutes what? In my opinion; strong government, strong armed forces and a society that’s aware of its background”** (Informant #1, personal communication, 11<sup>th</sup> September 2009).

Once again this position is strongly supported by business people who are involved in economic activities with Ukraine on the everyday basis. The issue of political situation cannot be avoided. ABB Grain Ltd. outlined that the Ukrainian government is very fragmented which often results in contradictory policies that negatively affect the society and the internal business environment (ABB Grain Ltd., personal communication, 14<sup>th</sup> October 2009).



### *6.3.1.3 Regulation and policy problems*

It is evident that in order to lower the risks faced by the Australian and other foreign investors it is necessary to improve current regulations, so that they correspond to the international standard (UkrSpirit, personal communication, 5th November 2009; UkrBeer, personal communication, 29th October 2009). As stated by DniproIndustrial, current regulations and policies provide very small distance between the government and operating businesses, which have very little autonomy (DniproIndustrial, personal communication, 25th August 2009). It is unclear whether policies and regulations in Ukraine are fair to all business actors. WoolStock provided the following comment on the issue: **“...regulation which is actually not like fair regulation because here we have fair independent regulation as such you know; I don’t know how independent those regulators are over there in terms of having government interference in Ukraine”** (WoolStock, personal communication, 11th September 2009). Similar views are also expressed by ABB Grain Ltd. Overall, the rules are very “dynamic”, but more so in a negative connotation.

The findings of this study support the research by the International Finance Corporation. By surveying mostly European entrepreneurs it was identified that the system of government regulations impedes sustainable economic development and competitiveness of the Ukrainian economy (IFC 2007). Overregulation, especially in the area of permits and taxation remain one of the most significant administrative problems. Taxation issues are also large, which is illustrated by constant and inefficient tax inspections as well as corruption. Export procedures, such as VAT refunds are also problematic for foreign actors (ABB Grain Ltd., personal communication, 14<sup>th</sup> October 2009). The findings by OECD are also in line with abovementioned positions (Refer to Section 3). This study confirmed the findings by IFC and OECD by looking at the Australian businesses operating in Ukraine.

#### *6.3.1.3.1 Overregulation*

Overregulation and difficulty to communicate with various government bodies in Ukraine was outlined by the World Bank and OECD since 2005. As a response to that, The Ukrainian Center for Foreign Investment Promotion (also known as InvestUkraine) was established by 2006 (Nikolaiko 2007). The purpose of InvestUkraine is improve investment image of Ukraine and assist foreign businesses with **“resolving bureaucratic issues with local officials and regulatory institutions through individual managers of major projects within the Government”** (National Agency of Ukraine for Foreign Investment and Development 2009). Moreover, InvestUkraine would consult foreign businesses on how to conduct business and assist with regulatory compliance. The efficacy and usefulness of the

“one-stop-shop”, at least from the perspective of the Australian businesses, should be challenged.

It is clear that in the past two years overregulation, unstable legislative environment as well as the inconvenience of communicating with various levels of government has not improved. The majority of the Australian businesses claim that it remains one of the most significant issues. The position of one of the interviewees argues that current policy and regulation issues illustrate of the transitional environment in Ukraine:

**“Their biggest problem is that they can only go so far because all of a sudden the old system kicks in. Now, until that old system stops kicking in you’re going to have these farcical situations and you’ve put it very well; more tax inspections but less income. ....**

**Well, yeah you know but I’d say that those that run that one-stop-shop must be pretty well connected because you couldn’t guarantee anybody anything until you were connected”** (Informant #1, personal communication, 11th September 2009)

It should also be stressed that ABB Grain Ltd. and UkrSpirit also confirm the difficulty that foreign businesses are facing due to regulation and policy issues.

#### *6.3.1.3.2 Tax*

The Ukrainian government should concentrate on developing a better environment for foreign companies and the reform of the taxation system underpins any improvement in that area (UkrSpirit, personal communication, 5<sup>th</sup> November 2009). MedTech and SoftwareEng also stress the issue of bureaucracy and taxation in particular. These are the main reasons that both of the companies refused to be present in Ukraine (MedTech, personal communication, 8<sup>th</sup> October 2009; SoftwareEng, personal communication, 8<sup>th</sup> October 2009). In case of ABB Grain Ltd., the Ukrainian government significantly delayed VAT refund and repaid VAT receivables in corn, all at the time when the Ukrainian Hryvnia was crashing.

Over the past 10 years it is hard to say that taxation system has had any significant improvement. The case of OilExplore illustrates that Australian companies had similar issues also in 1995-98:

**“Tax reporting... – person always sitting at the tax office to submit the reports. It’s hard to keep up with all the developments, lots of administrative issues and consultancy was taken and at that stage the company had no revenue at all”** (OilExplore, personal communication, 12th October 2009).

#### *6.3.1.4 Weak rule of law: Corruption*

Corruption is also a highly significant obstacle that all Australian businesses have to deal with when operating in Ukraine. A detailed discussion of the weak rule of law and its

implications is presented in Section 3. This section will illustrate how the Australian businesses are affected by the lawlessness of the Ukrainian business environment.

While in some cases corruption is not a significant barrier for business operations that is not the case for Ukraine. The main characteristic of the Ukrainian system is that the informal fee you are paying does not provide any kind of guarantee or stability. This view is supported by the vast majority of interviewees. It is evident that over the past 18 years corruption remains highly detrimental to business practices between Australia and Ukraine.

The following views are expressed by the participants:

**“In previous times if I paid the fee I at least knew that there was going to be an outcome or I knew what the fee would be. ... The issue is, ‘I can pay the fee, there’s no guarantee that anything will happen and secondly I don’t know when the fee’s going to finish because there’s a fee on top of the fee’. ... The problem is you have a system you know. We don’t want to politicise the situation ... and you’re not too keen about changing the system because you’re making money”** (Informant #1, personal communication, 11th September 2009).

**“Corruption is a minor factor ... as long as there is guarantee and relevant stability, which is not the case in Ukraine”** (DniproIndustrial, personal communication, 25th August 2009)

**“We will not be present in Ukraine to avoid the lack of rules and overcome many other problematic issues while working there”** (SoftwareEng, personal communication, 8th October 2009)

Furthermore, corruption poses the highest threat to listed companies that cannot afford making any informal payments. In case of ABB Grain Ltd., the company cannot be associated with any corrupt practices which in turn significantly delays negotiation process in Ukraine. Cooperation with local businesses is often avoided by foreign listed companies to prevent the involvement in “informal” arrangements.

Further this section provides illustrations of the following obstacles: work ethic, difficulty to negotiate and strike a deal, geographic distance as well as the image of Ukraine on the international arena. However, it should be stressed that instability of the business environment in Ukraine remains the main obstacle to a greater economic cooperation with Australia.

### *6.3.2 Minor issues*

#### *6.3.2.1 Culture: Work ethic*

Australian businesses express concerns about work ethics in Ukraine and claim that culturally people do not understand the main principles of capitalism. This notion is explained by the following dialogue:

**“he sort of seemed to have this mentality – oh I have bought a house therefore you should be paying me more. I don’t know where that comes from. It is a misconception of what capitalism is about. I pay him on his productivity in the business and then he does what he wants with the money.”** (WoolStock, personal communication, 11th September 2009)

In the same vein, EuroBeverages argued that Ukrainian suppliers simply do not understand the role of performance, which is how all modern businesses operate. The position of ABB Grain Ltd. also outlines relatively weak work ethics. On the other hand, MedTech and SoftwareEng provide examples where individuals from Ukraine have a very strong passion to be part of an organization that allows them to employ their skills and knowledge. **“Good brain, hard-working, good work ethic in younger people, all ingredients of doing something are there in Ukraine, but you have to go through so many problems to harvest these seeds and to make them grow”** (MedTech, personal communication, 8th October 2009).

#### *6.3.2.2 Difficult to deal and negotiate*

Just less than half of the interviewees experienced difficulties in communicating and negotiating with Ukrainian businesses (The summary of findings is presented in Table 3.1). Concerns were expressed by DniproIndustrial; it was noted that the executives involved in negotiations had very limited knowledge of economics and thus it was extremely difficult to communicate and achieve any agreement (DniproIndustrial, personal communication, 25<sup>th</sup> August 2009).

EuroBeverages express a similar position:

**“They are not very reliable... Sometimes I cannot find the container, simply because they did not get to prepare the documents properly or inform me about the arrival. Extremely unreliable, if someone offers a dollar extra, they will go for it, not paying attention to any previous dealings”** (Translated from Russian, EuroBeverages, personal communication, 8th October 2009)

At the same time, there are views that the issue of communication will not remain problematic for Australian businesses. The position by informant #1 on the issue is as follows:

**“There are young people who are budding politicians. They’re people who now understand how normal business operates ... and who are trying to do it the right way”** (Informant #1, personal communication, 11<sup>th</sup> September 2009)

#### *6.3.2.3 Geographic distance*

Geographic distance is a relatively minor obstacle for economic dealings between Australia and Ukraine. It should be noted that both, Ukrainian and Australian companies, mention that as a factor that affects or limits current economic dealings. ABB Grain Ltd. strongly believes that for Ukrainian businesses it is easier to cooperate with Europe than Australia. Also, MedTech expressed some concerns regarding the distance. Both of the Ukrainian companies, UkrBeer and UkrSpirit outline that the distance makes it very lengthy (40 days) to deliver the products to Australia. Moreover, it limits the variety of products UkrBeer can supply to Australia and forces companies to minimise the logistic costs.

#### *6.3.3 Image of Ukraine on the international arena*

It is clear that the international image of Ukraine can create obstacles for further bilateral ties with Australia. As already illustrated, ABB Grain Ltd. had difficulties obtaining finance from major banks. Current poor microeconomic performance is further weakening the perceptions about Ukraine on the international arena.

Strong views were expressed about the lack of national identity and the fact that Ukraine is often mistaken for Russia. To thoroughly illustrate this argument the following quotes are provided:

**“Ukraine has yet to establish itself. It’s always still been living in the shadow of Russia. What we’ve been trying to do is in a sense say that Ukraine is now 18 years of independence, that Ukraine is a worthy partner to do business with.**

**Where does Ukraine sit internationally, ...pro Europe, pro Russia?**

**...you’ve got to take your hat off to them [referring to Russian Federation] in terms of the way they do public relations ... they know how to do public relations. And their politics in the sense of public relations, constantly interferes with what happens in Ukraine”** (Informant #1, personal communication, 11<sup>th</sup> September 2009).

**“You see the difference between Poland and Ukraine is that Poland has always had a western orientation. ...I think that one problem with Ukraine is always the case is they just have difficulty, in this sort of society, this far away from that, literally conceptualising what it is. They know what Russia is ... ‘what is Ukraine I thought they were all Russians’”** (WoolStock, personal communication, 11<sup>th</sup> September 2009).

## **6.4 Obstacles of the Australian business environment for further development of bilateral relations with Ukraine**

It is clear that from the Australian side the obstacles to a greater economic cooperation with Ukraine are insignificant. Nevertheless, some minor obstacles for Ukrainian businesses to cooperate with Australia will be discussed in this section. The summary of the findings is illustrated by Table 6.2.

### *6.4.1 Minimal Interest in Ukraine*

One of the major problems for dealings with Australia is the fact that there is a very little interest in Ukraine. Perhaps, this issue is applicable to both countries, Australia and Ukraine. The relevance of this factor is best described by providing the following quote: **“If you try to identify those who would be interested to run the business between Australia and Ukraine, you will find that no one is really concerned about the matter”** (Informant #2, personal communication, 9th September 2009). Ukraine and Australia has to move away from weak political discussions and start making real steps towards the improvement of bilateral relations. This view is supported by the following interviewee:

**“Australia and Ukraine have to ultimately say to themselves, ‘Do we want a relationship?’**

**My position is this ... that you [refers to Austrade] give us a minimal amount of money to open an Austrade office or to be your representative”** (Informant #1, personal communication, 11th September 2009).

#### *6.4.1.1 Unwillingness to accept offshore risks*

The minimal interest of Australia to conduct business with Ukraine can be explained with its unwillingness to accept higher risks. This has caused difficulties for the Australian businesses to expand its operations and explore the benefits that Ukraine has to offer. ABB Grain Ltd. is a very successful example of the economic ties between the two countries, yet, at the early stages the company found it difficult to assure that in their case the benefits of expanding to Ukraine outweigh the potential risks (ABB Grain Ltd., personal communication, 14th October 2009). WoolStock also expressed similar views:

**“It was too hard for them, too exotic, too far away to even do that because they thought it will go to nowhere”** (WoolStock, personal communication, 11<sup>th</sup> September 2009).

### *6.4.2 Funding*

The issue of funding and the relevant example from ABB Grain Ltd. is presented in Section 6.3.1.1.2

#### *6.4.3 Demand and market size*

UkrSpirit argued that while establishing export operations with Australia they had to take into account the demand for their products. The fact that Australian consumers purchase more wine and other beverages with small content of alcohol was carefully studied by the company. The culture of alcohol consumption in Australia significantly differs to Ukraine. Overall, UkrSpirit believes that there are strong perspectives for further growth of demand for its products, which is underpinned by the introduction of higher taxes for weak alcoholic beverages. On the other hand, UkrBeer expresses concerns about its perspectives on the Australian market and claims that there are better opportunities in the United States (UkrSpirit, personal communication, 5<sup>th</sup> November 2009, UkrBeer, personal communication 29<sup>th</sup> October 2009).

#### *6.4.4 Geographic distance*

The implications of geographic distance for both Australia and Ukraine are discussed in Section 6.3.2.3.

#### *6.4.5 High level of tax on specific products*

Concerns were expressed regarding the high level of tax on strong alcoholic beverages by UkrSpirit. However, this cannot be regarded as a significant issue that will affect a wide range of Ukrainian companies that conduct business with Australia. UkrSpirit outlined that import taxation forces the company to remain highly competitive (UkrBeer, personal communication, 29<sup>th</sup> October 2009; UkrSpirit, personal communication, 5<sup>th</sup> November 2009).

UkrSpirit, UkrBeer and EuroBeverages also noted the ease and transparency of Australian taxation and other policies.

### **6.5 Recommendations**

#### *6.5.1 Entry mode*

While taking into account the characteristics and risks of the business environment in Ukraine it can be stated that forming a joint venture is the most convenient and effective mode to enter the market. From the sample of the companies questioned all successful cases either formed joint-ventures or established import operations from the Ukrainian suppliers. UkrSpirit suggests that **“the best form of ownership would be a joint-venture, where foreign investor meets the financial obligations and local Ukrainian companies, while having a better knowledge of the operational context, will concentrate on the operations**

**of the company”** (UkrSpirit, personal communication, 5<sup>th</sup> November 2009). However, even in that case interviewees stress the importance of laissez-faire capitalism in Ukraine. As discussed in Section 6.3.1.3 currently private enterprises have very little autonomy that is undermined by the state control.

The case of ABB Grain Ltd. ideally illustrates the benefits of joint-venture as an entry mode. It was crucial for ABB Grain to find a partner who has experience of operating in the Ukrainian business environment. ABB Grain Ltd. commented that forming the joint venture with Soufflet had bilateral benefits. Soufflet has had 8 years of presence in the Ukrainian market. At the same time, ABB Grain Ltd. had strong export marketing arm and could provide relevant customer base for Soufflet (ABB Grain Ltd., personal communication, 14th October 2009). Nevertheless, the difficulty of finding a company that can initially become a partner should not be underestimated.

#### *6.5.2 Better diplomacy between Australia and Ukraine will stimulate greater economic cooperation*

The following quote provides a good summary on how effective is the diplomacy between the two countries:

**“Delegations and organizations that are meant to develop further trade and investment relations between Australia and Ukraine talk a lot, however, without any actions or results on their behalf. These people do nothing and simply come here to have a holiday, it is better to spend this money on one of the schools in Ukraine.”** (Informant #2, personal communication, 9th September 2009).

A recent parliamentary delegation from Ukraine to Australia only rashly addressed some of the problems as well as perspectives of the further development in trade and investment. **“The delegation simply lied about the future developments and current problems”** (Informant #2, personal communication, 9<sup>th</sup> September 2009). Arguments and propositions presented by Ukraine were off the top of the head. As an example, the discussion arose that Ukraine could supply cricket bats to Australia and about the prospective of such cooperation. However, up until now nothing has been done and at the time when the argument was presented Cricket Association of Australia knew nothing about the development and was not contacted or approached by the Ukrainian side.

There is strong evidence to argue that the bilateral communication between Australia and Ukraine is lacking. This position is expressed by almost all interviewees and while it is agreed that businesses want to do as little with government as possible, there is a need in a better dialogue between the two countries.



The Australian Federation of Ukrainian Organisations acted as a strong advocate between the Australian and Ukrainian governments, it also attempts to facilitate discussions between businesses and promote the potential for the Australian businesses in Ukraine. At the same time, the Federation believes that the Ukrainian Embassy should be more involved in these issues as it is one of its main obligations. ABB Grain Ltd. also highlighted the minimal interest of the Ukrainian Embassy to initiate discussions/workshops that can contribute to the exchange of knowledge between the two countries.

None of the Australian businesses received any help the government of either countries. It is crucial to facilitate business cooperation between Australia and Ukraine:

**“There’s no vehicle to encourage it. That usually starts at government level... Businessman will do business wherever there are opportunities. They’re not going to pull out, they’re not going to say “I don’t like Ukrainians”.**

**Initially, if there is, it’s a government relationship, the fact we don’t have... if you just talk about Australia specifically the fact that we don’t have an Ambassador in the Ukraine is sad to me. But that’s where it’s got to start.”** (WoolStock, personal communication, 14th October 2009)

As already discussed in Section 6.4.1, Australia also has a minimal interest in facilitating business activities with Ukraine. The position is strongly argued by informant #1, who refers to the fact that Austrade has no representative or office in Ukraine.

## **7. CONCLUSIONS**

The economy of Ukraine is still at its transitional stage, lack of transparency, highly volatile environment, with unstable macroeconomic performance, political system and corruption make it a very risky journey for the Australian companies. Moreover, Ukraine lacks independent image on the international arena and the baggage of the command economy is still visible. The current situation in Ukraine should improve, but not without the effort and stability at the government level. The current situation is discouraging, especially when taking into account the vast potential that Ukraine can offer. The development of the new economy is undermined with the ignorance of the Ukrainian government to facilitate business activity and foreign investment.

The Ukrainian Economy can be efficient, which is illustrated by stable growth during 2004-07. Even so, it is currently severely hit by the global financial crisis and requires international support. As already illustrated, significant market reforms are crucial in Ukraine. It is absolutely essential to develop reliable policies and regulations, promote business autonomy, fight corruption and “rent-seeking”, facilitate and assist foreign actors to

overcome instability and high level of risk present within the country. Further work is needed to meet the standard of WTO countries; it is also essential to progress with the developments on the EU free trade agreement. It is clear that bilateral business ties with Australia will be weakened unless there is a prompt response to resolve current deteriorating situation.

Based on the evidence collected, the Australian companies can be advised to consider a joint-venture as an entry mode into Ukraine. It is highly important to find a reliable partner who will assist with business activities in Ukraine. Local operators or foreign firms who have a lengthy presence in Ukraine already gained necessary experience, networks and contacts that are crucial to enjoy a better level of stability. Risk exposure must be minimised at the earliest stages. Due to highly volatile environment it is often impossible to predict significant barriers of the “dynamic” system.

Australian business environment, on the other hand cannot be considered as a barrier to bilateral business relations with Ukraine. The vast majority of companies identify no significant barriers for further cooperation with Ukraine on the Australian side. Nevertheless, minimal interest in Ukraine and unwillingness to accept risks contribute to deteriorating business relations with Ukraine. Australian companies experienced significant issues with obtaining funding for business projects in Ukraine. It is crucial to consider Ukraine as a distinct country with the business environment specific to its internal conditions.

Better dialogue between the Australia and Ukraine is essential to support bilateral relations between the countries. This obstacle is relevant to both sides. It is necessary to consider whether the two countries want to advance in bilateral business relations and if the answer is positive, relevant actions should be taken. Bilateral communication is lacking, there is no Austrade office in Ukraine, and neither there is an Australian Embassy. The business activity is highly reliable on the developments at the higher government levels. Government assistance and support can be seen as the strongest instrument to overcome the barriers between the two countries.

### **7.1 Limitation and Recommendations for Future Research**

It is clear that Ukrainian companies are underrepresented in this study. Therefore, the barriers of the Australian environment are not adequately analysed. Overall, it is necessary to include a larger sample to avoid generalisations and present an argument in line with the broader context. This study also collected data on industry-specific obstacles, however, further investigation is necessary to present coherent findings. Moreover, the role of networks and contacts is not addressed, which is a significant limitation. Finding a reliable business partner is essential for stable business operations in Ukraine and thus the discussion

on the role of networks cannot be avoided. While this study did not accentuate the role of networks and how they influence business operations, it should be mentioned that at least one third of the interviewed companies would not have being able to establish business operations in Ukraine without relevant connections.

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