

Globalization and Ukraine: Vector's Aspect of the Further Economic Development

by

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Abstract. In the last years the humanity assists to the fundamental changes in economy no matter the level from which is regarded. These changes are so fast and intensive that many times the humanity is confronting also with adaptation difficulties and also with the collapses of some value systems which have proved themselves incompatible with new realities to the world level. So, we've become the witnesses of a world in which the commercial bounds and the capital fluxes between countries have grown so much that the globalization of the world economy is a reality. The globalization is a term used to describe a multi-causative process which has as result the fact that the events which takes place in some part of the globe have more and more wide repercussive on the societies and on the problems from other parts of the globe. It influences all aspects of the life, including economic development. Therefore, it's very important to investigate the influence of this factor in any economic research.

Keywords: EU, globalization, ratings, Post-Soviet countries, Ukraine

JEL Classification: E22; F21; H5

1 Introduction

The main vectors of Ukraine's domestic and foreign economic policy over the last decade and a half have been the so-called European and the Russian vectors. The former presupposes orientation toward Europe and a goal of eventual membership in the European Union. The latter implies orientation toward closer economic ties with Russia. After the Orange Revolution, the new Ukrainian leadership affirmed the EU membership as its first priority. However, since 2004, Ukraine has not moved any closer to the EU, but managed to isolate itself from Russia. A significant break-up of the economic ties with Russia has been a big drawback in Ukraine's economic policy and contributed to the declining rates of growth. It mainly occurred because the new Ukrainian leadership has opted to treat the two "vectors" as alternates and made decisions that were definitely driving Ukraine away from Russia. So, *the aim* of the article is to identify the dependency between the countries' attractiveness to foreign investors and their position in international ratings and, if there the hypothesis is right, characterize the best vector for the further Ukrainian economic policy.

The previous researches connected to this topic were not so global and concentrated mainly on: the position of Ukraine in international ratings [2], dependency of the countries' attractiveness to foreign investors from the position in one international rating [1].

The main methods to be used in the article are: quantitative (statistical, regression analysis) and analytical.

2 Main content

In the modern world all foreign economic relations should be based on market-driven decisions. Among other things, this means prevalence of money transactions over barter. It is well-known that barter transactions have been widespread in the early stages of transition from centrally planned economies to the market system. Barter still exists in relations between countries of the former Soviet Union. Economic theory tells us that relations based on barter are inefficient, because they lock-in efficient and inefficient enterprises, and in many cases efficient enterprises subsidize inefficient ones. Many questions arise in this regard. How come that the country which is so much dependent on Russian and the entire post-Soviet market could not recognize it? It is a reality of time that many

Ukrainian products are only competitive in post-Soviet space but not competitive in the world markets. Therefore, strategically it was necessary to find products that are associated with the Ukraine's comparative advantage first, then find ways to sell these products through world markets, keep selling other products in the post-Soviet space.

In the research there were chosen 2 well-known ratings, which are published every year, starting from 2006: the Index of Economic Freedom - X Variable 1[5] and the Corruption Perceptions Index - X Variable 2[6]. They reflect the main principles of the changes in human values, the progress of the reforms, the effectiveness of the state economic policy and a lot of other factors. Thus, they may help us with the main goal of the research – to indicate the best vector of the further economic reforms in Ukraine: whether it is the scenario of the European Union, pro-Russian countries or its own way. Moreover, it should be noted that data on these ratings are available for all countries. We couldn't use other ratings because of restrictions regarding the period of the research or they were not provided for all countries from our sample. These kind of restrictions were noticed regarding the Global Competitiveness Index[4] and the Doing Business Rating [3] and some other ratings.

For the estimation of the model we use data compiled from several sources. In addition to the indexes described above, we use data on foreign direct investment and population. All of the variables were taken from the World Bank data base [7]. As noted, data on seven countries over the years 2006-2012 are included in the data set.

As for the Index of Economic Freedom, The index scores nations on 10 broad factors of economic freedom using statistics from organizations like the World Bank, the International Monetary Fund and the Economist Intelligence Unit: Business Freedom; Trade Freedom; Monetary Freedom; Government Size/Spending;; Fiscal Freedom; Property Rights; Investment Freedom; Financial Freedom; Freedom from Corruption; and Labor Freedom[5]. The 10 factors are averaged equally into a total score. Each one of the 10

freedoms is graded using a scale from 0 to 100, where 100 represents the maximum freedom. A score of 100 signifies an economic environment or set of policies that is most conducive to economic freedom.

The 2012 Corruption Perceptions Index draws on 13 different surveys and assessments from 12 different institutions[6]. The institutions are the African Development Bank, the Bertelsmann Foundation, the Economist Intelligence Unit, Freedom House, Global Insight, International Institute for Management Development, Political and Economic Risk Consultancy, Political Risk Services, the World Economic Forum, the World Bank and the World Justice Project.[6]

Countries must be assessed by at least three sources to appear in the Index. The 13 surveys/assessments are either business people opinion surveys or performance assessments from a group of analysts. Early Corruption Perceptions Indexes used public opinion surveys.

Thus, the above-mentioned ratings have scientific importance, are used in macroeconomic overviews by economists all around the world and, according to our hypothesis, can influence the foreign direct investment.

The sample includes data on countries' variables on which the observations covers a relatively short period of time – seven years. This is not ideal time coverage to capture fixed effects of these variables. The reason is that the data may have been subject to short-term fluctuations. It would certainly have been preferable for us to use longer time series but, unfortunately, we were seriously constrained by data availability and resources.

We chose 7 countries to compare with Ukraine. The choice was made according their geographical position, territory, population and current political and economic position in the world. There were 3 blocks of countries formed (table 1).

Table 1. Blocks of the countries

Block 1	Block 2	Block 3
Lithuania	Belarus	Poland

Latvia	Uzbekistan	Romania
	Kazakhstan	

In this research we concentrated our attention to the problematic of the economic development of the post-Soviet states, also commonly known as the Former Soviet Union and position of Ukraine regarding the future directions within geo-political and geo-economic development. There are the 15 independent states that emerged from the Union of Soviet Socialist Republics in its dissolution in December 1991. The three Baltic states restored their

independency on the basis of state continuity; while the remaining 12 republics are deemed to have seceded from the Soviet Union and are thus referred to as the Newly Independent States (NIS). The NIS subsequently formed the CIS and most joined CSTO, while the Baltic states eschewed that path and instead joined both the European Union and NATO.

After the collection of data on the foreign direct investment and population we calculate the amount of foreign direct investment per person (Y) (table 2).

Table 2. Foreign direct investment (per 1 pop, US\$)

		2006	2007	2008	2009	2010	2011	2012	2012 /2006	2009 /2006
Block 1	Lithuania	542,12	572,93	585,15	19,76	243,4	477,86	282,02	0,52	0,04
	Latvia	726,85	1020,17	556,46	41,69	169,72	712,28	480,53	0,66	0,06
Block 2	Belarus	37,17	189,02	229,64	197,43	146,79	422,46	152,45	4,10	5,31
	Uzbekistan	6,57	26,24	26,04	30,32	57	50	37,01	5,63	4,61
	Kazakhstan	415,47	716,6	1006,44	822,88	707,64	839,62	825,31	1,99	1,98
Block 3	Poland	513,96	618,07	385,28	338,96	363,4	490,76	87,09	0,17	0,66
	Romania	526,55	460,44	646,52	225,51	137,14	117,98	117,73	0,22	0,43
	Ukraine	119,77	212,67	235,91	104,57	141,59	157,68	172,1	1,44	0,87

As we can see from the Table 2, the period of the financial crisis didn't influence the non-EU countries according the dynamic of the foreign direct investment. It means that there are a lot of other factors to be more influential, than the ratings.

Also it should be indicated that the situation with the foreign direct investment for Ukraine is a bit different. The main "source" of the foreign

direct investment is return of the offshore money (in particular, from Cyprus), which was withdrawn from the country to avoid taxation. This factor is visible in regression analysis.

In order to create a background for an analytical analysis, we use regression analysis for every country, including Ukraine. The results are provided below in table 3.

Table 3. Results of the regression analysis

	Block 1		Block 2			Block 3		Ukraine
	Lithuania	Latvia	Uzbekistan	Belarus	Kazakhstan	Poland	Romania	
Regression Statistics								
Multiple R	0.932395	0.398038	0.946006	0.12699	0.311327	0.701723	0.838606	0.328003
R Square	0.86936	0.158434	0.894927	0.016126	0.096925	0.492415	0.70326	0.107586
Adjusted R Square	0.804041	-0.26235	0.842391	-0.47581	-0.35461	0.238622	0.55489	-0.33862
Standard Error	94.36091	379.2512	6.643345	142.0297	211.7456	147.7228	147.4532	55.15081

Observations	7	7	7	7	7	7	7	7
ANOVA								
<i>Significance F</i>	0.017067	0.708233	0.01104	0.968007	0.815545	0.257643	0.088055	0.796403
<i>F</i>	13.30929	0.376522	17.03444	0.032781	0.214655	1.940226	4.739909	0.241112
Coefficients								
Intercept	-14605	-5914.96	271.369	689.9651	-1279.39	1169.916	5637.887	58.29579
X Variable 1	244.0328	81.82799	-2.04765	-12.0699	40.95178	0.079537	-93.371	-2.52384
X Variable 2	-478.121	213.1767	-79.2395	32.11435	-183.169	-159.122	138.9195	91.69683
t Stat								
Intercept	-3.55863	-0.614	5.058352	0.349439	-0.27498	0.436349	3.189733	0.170086
X Variable 1	4.257806	0.513427	-1.86868	-0.25594	0.509854	0.001409	-2.62486	-0.27502
X Variable 2	-3.11968	0.367067	-4.84335	0.163011	-0.58598	-0.85959	0.639076	0.660315
P-value								
Intercept	0.023615	0.572419	0.007189	0.744381	0.796952	0.685102	0.033225	0.873199
X Variable 1	0.013076	0.63471	0.135038	0.810617	0.636997	0.998943	0.0585	0.796921
X Variable 2	0.035537	0.732164	0.00838	0.878414	0.58936	0.438481	0.557535	0.545139
Standard Error								
Intercept	4104.093	9633.522	53.64772	1974.493	4652.706	2681.148	1767.511	342.7432
X Variable 1	57.31421	159.376	1.095775	47.15824	80.32056	56.44456	35.57178	9.176883
X Variable 2	153.2593	580.7576	16.36045	197.0066	312.5865	185.1135	217.3757	138.8683

Lithuania: The multiple regression form of the model is:

$$y = -14605 + 244.0328x_1 + -478.121x_2$$

The results of the analysis show that the R Square is high – 86.9%. The Significance of F = 0.017, there is only a 2% chance that the Regression output was merely a chance occurrence. So, there is dependency between the foreign direct investment and a position in the rating of Lithuania.

Latvia: The multiple regression form of the model is:

$$y = -5914.96 + 81.82799x_1 + 213.1767x_2$$

As for Latvia, the R Square is just 16% and the Significance of F is 0.71, which is very high. So, we can't make any objective conclusions about a relationship between foreign direct investment and place in a rating for Latvia.

Uzbekistan: The multiple regression form of the model is:

$$y = 271.369 + -2.04765x_1 + -79.2395x_2$$

The results of Uzbekistan in this research show that this country has the highest correlation between the changes in the ratings and the foreign direct investment, which is adjusted by the R Square of 89%. Also the P value (except X Variable 1) is less than 0.05. It means that the influence of X Variable 1 is not so significant.

Belarus: The multiple regression form of the model is:

$$y = 689.9651 + -12.0699x_1 + 32.11435x_2$$

The results of the regression analysis for Belarus show that there is almost no connection between the foreign direct investments to the country and its position in ratings. The R Square of 2% and the Significance F of 97% indicate it very clearly.

Kazakhstan: The multiple regression form of the model is:

$$y = -1279.39 + 40.95178x_1 + -183.169x_2$$

The high value of the Significance F and the R Square of 10% show us that there is no connection between the foreign direct investments to Kazakhstan and its position in foreign ratings.

Poland: The multiple regression form of the model is:

$$y = 1169.916 + 0.079537x_1 + -159.122x_2$$

The Significance of F = 0.25. It means that there is a 25% chance that the Regression output was merely a chance occurrence. It doesn't allow us to make a conclusion that there is any dependency between foreign direct investment of Poland and its place in ratings. Moreover, the R Square is just 49%, which is not very high.

Romania: The multiple regression form of the model is:

$$y = 5637.887 + -93.371x_1 + 138.9195x_2$$

The R square is 70% and the Significance of F is higher than average. It means that there is some dependency between foreign direct investment of Romania and its place in ratings. But we should take into consideration that there is a 8.8% chance that the Regression output was merely a chance occurrence. Moreover, the P value of X Variable 1 and 2 is higher than 0.05.

Ukraine: The multiple regression form of the model for Ukraine is:

$$y = -58.29579 + -2.52384x_1 + 91.69683x_2$$

From the analysis we see that there is no big relationship between the foreign direct investment and a position in the rating, as far as R Square is just 11%. It means that maybe other variables will explain the variability as well (for example internal factors, which are not included to the indexes). Also we have to take into consideration that the standard error is very high and the P value is more than 0.05. Thus, we can't reject the null of a zero slope and conclude there is no relationship between foreign direct investment and place in a rating for Ukraine. A high Significance of F also adjusts the output.

3 Conclusion

Ukraine is one of the biggest, but also the second poorest country in Europe. Given its territorial size, its geographic position, its almost 46 million population and its role as the main transit state for Russian oil and gas exports to central and western Europe, Ukraine has been a critical strategic factor for Euro-Atlantic and Eurasian security in the two decades of its independence. Today, it stands at a critical crossroads between developing a more open society increasingly integrated into the European space of democracy, prosperity and market-based economics grounded in respect for human rights and the rule of law, or an increasingly autocratic system, mired in the economic stagnation and political instability

that is historically characteristic of Europe's borderlands.

Nowadays it's very important for the country to have clear future directions within geo-political and geo-economic development. In this research we checked the hypothesis regarding the correlation between the countries' attractiveness to foreign investors and their position in international ratings. Due to the initial conditions, with the help of this research we wanted to elaborate the recommendations regarding the vector of further economic development of Ukraine: the scenario of the European Union, pro-Russian countries or its own way.

The results of the regression showed us, that from 8 countries (including Ukraine) only 2, Lithuania and Uzbekistan, have this dependency. Moreover, the influence of the ratings on the foreign direct investments in Ukraine is not very high. It means that there are a lot of other factors, which are more important for the country. The general tendency is that the position of a country in the ratings may be more or less influential factor (within 10%) for foreign investors.

As for the first block of the countries, we can see that the investors to the economy of Lithuania, among other factors, take into consideration the position of the country in ratings. But the investors to Latvia are directed by other factors more. There is a clear correlation between the foreign direct investment and the position of Uzbekistan in ratings. As for the other countries from the second block, we hardly see any dependency there. The investors to Poland and Romania are not driven by the factors within the indexes as well.

Furthermore, the results of the research didn't provide a scientific background to make a conclusion regarding the further directions to improve the investment attractiveness of the country regarding the initial 3 blocks of directions. Ukraine should choose its own way to build the strategy on improving Ukraine's investment attractiveness. It should concern not only the position of the country in the world ratings, but mainly the indices of sustainable economic and political development, such as:

monetary and fiscal policy, the level of corruption in the country, infrastructure, court systems reform, land reform, administrative leverage, social safety net etc.

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