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The impact of foreign investment on strengthening the security of the national economy of Ukraine and investment guidelines for Ukrainian-Polish cooperation

Abstract. The article examines the theoretical foundations of the category of foreign direct investment and identifies their characteristic features. The importance of foreign investment is substantiated, and both positive and negative consequences of FDI for the country's economy are identified. The research investigates the dynamics of the inflow and the geographical structure of foreign direct investment by country of receipt of investment, presents the largest investor countries and the most attractive sectors for investment in the Ukrainian economy, and evaluates the degree of deterioration in the investment attractiveness of the national economy. The features of Ukrainian-Polish investment cooperation are studied, and priority directions for developing investment activity are discussed.

Keywords: foreign direct investment, investment activity, state security, Ukrainian-Polish cooperation

Introduction

The rapid growth of foreign direct investment (FDI) in many developing countries and countries with economies in transition indicates that inward FDI has become much more important than a few decades ago. These economic changes were accompanied by political shifts regarding FDI: many developing countries and those in transition abandoned Marxist and post-Marxist concepts that had negatively assessed FDI and became more favorable to foreign investors. Most of these countries have introduced various incentives to attract FDI, the primary purpose of which is to create a favorable business climate where foreign investors can feel confident in the legal and financial system of the country and profit from economically stable businesses (Ginevičius and Šimelytė, 2011). However, several external risks, including pandemics, geopolitical risks, and war, significantly impact the global financial system and change the conditions of the market game for its participants. Soon after Russia's aggression against Ukraine,

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companies began to operate under great uncertainty, which led to the freezing of investment plans and the disorganization of business processes. Central investments were stopped, and companies decided to either invest in other regions or abandon investments altogether (Kopiński, 2022, p. 25). The war was a severe test for the economy. Given the challenging macroeconomic environment and the slowdown in global economic growth, it is rather complex to determine investment strategies in Ukraine during the war.

Without significant reforms, investment policy improvement, and capital security guarantees, it would be impossible to develop business and attract foreign investment to Ukraine. Poland is one of the strategic partners of Ukraine. Therefore, Ukrainian-Polish cooperation is an object of attention from the point of view of identifying reserves for improving economic relations between Ukraine and member countries of the European Union at the present stage of European integration transformations. It applies to both economic activity in general and its individual components, in particular investment.

The study aims to identify trends, diagnose problems, and develop promising ways to attract foreign investment into the Ukrainian economy. It is also expected to analyze the features of the development of Ukrainian-Polish cooperation in the investment sphere and identify priority areas for further cooperation.

Literature review

Investment activity is a key factor in the development of any country, and during martial law, it requires even more attention and becomes a priority strategic task to ensure the normal functioning of the state's economy. Research on the problems of foreign investment includes works of scientists such as Rostow (1971), Kovel (2024), Puchalska (2015), Kopiński (2022), Ginevičius and Šimelytė (2011), Savchenko and Stepaniuk (2024), Kozachenko (2016), Savitska and Fugelo (2018), Sheremetinska and Kavchuk (2016), Ancyparowicz (2009) and others.

Attracting investment into the economy of any country is one of the main objectives of economic policy. According to Rostow (1971), countries with insufficient domestic resources can accelerate their economic development due to the influx of foreign direct investment. The use of capital in this form is a type of linked transaction that occurs at three levels: capital, technology and experience. Therefore, they should be considered not only as additional capital but also more broadly as the transfer of various production factors, including technological, managerial, and marketing skills, which play an essential role (Ancyparowicz, 2009).

The flow of FDI makes it possible to implement large technological projects, more effectively use the existing resources and industrial potential, modernize the technological base through the introduction of the latest technologies, and contribute to the expansion of international relations. This, in turn, leads to an increase in gross value added and the development of all spheres of the country's economic life (Kovel, 2024).

Foreign direct investment influences domestic investment by stimulating domestic producers to cooperate and compete with foreign-owned companies. Businesses facing bankruptcy or hostile takeover try to keep up with technological advances to reduce costs, improve product quality, and expand product offerings (Puchalska, 2015).

According to the Law of Ukraine „On the Regime of Foreign Investment” (Zakon..., 1996), foreign investment in Ukraine means all types of assets that are invested directly by foreign investors in objects of investment activity under the current legislation of Ukraine.

The Ministry of Finance (Priami inozemni investytsii (PII) v Ukrainu) interprets foreign direct investment (FDI) as long-term investments of certain material assets by non-resident companies in the country’s economy. Foreign direct investment is the most desirable form of investment for all developing economies because it allows the implementation of large-scale projects.

Among the various sources of foreign capital, foreign direct investment (FDI) is considered the most profitable and safe form of international investment, as well as financing of restructuring and development processes. Under favorable systemic and structural conditions, they are the most effective way to gain direct access to modern technologies in production and management and external markets (Janasz, 2011).

Having analyzed the works of scientists (Rogach, 2005; Teslia, 2009; Puchalska, 2015), it can be noted that attracting foreign investment to the country has both positive and negative effects. The positive ones include:

1. Economic growth. Creation of new jobs, development of industry and social infrastructure, improvement of the balance of payments, development of export potential and reduction of dependence on imports, additional capital, access to new markets, additional tax revenues.
2. Development of human resources. Typically, attracting investment is accompanied by the education and training of new local personnel, which increases the skill level of the workforce.
3. Technological progress. Transfer of new technology, transfer of management skills, marketing know-how.
4. Expansion of international relations. Attracting investment increases the country’s attractiveness to foreign partners and contributes to the development of international cooperation. It enforces better connections with the market at the international level and inclusion in international structures.

However, along with the positive consequences, foreign investments can pose certain threats, such as the exploitation of raw materials and environmental pollution, an increase in the country’s dependence on foreign capital, a decrease in the competitiveness of domestic producers, a reduction in tax revenues through capital transfers; deterioration of the balance of payments due to a rise in imports and a drop in exports by crowding out local exporters.

For Ukraine, the development of the investment market is decisive. Being an integral component of transformational changes in the country’s economy, it ensures effective integration of the national economy into the world economy, promotes the

spread of innovation, and increases labor productivity. Cooperation between Poland and Ukraine solves the problems of attracting investment, from coordinating foreign policy principles to cross-border cooperation, which is relevant for both countries with common historical, political, and economic backgrounds (Kozachenko, 2016).

Research methods

The theoretical basis of the study is the works of domestic and foreign scientists who analyze the features of investment activity, the problems of attracting and developing foreign investments, as well as the dynamics and structure of investments. During the research process, both general scientific and specialized methods of cognition were used. Among them is the method of scientific generalization – to determine the prospects for attracting foreign investment in the Ukrainian economy; systematic approach – to summarize FDI inflows to Ukraine, their distribution by sectors of economic activity and by country; abstract-logical method and methods of theoretical generalization – to study the essence of FDI and their positive and negative impact on the country's economy; graphic method – to schematically reflect the main theoretical and practical provisions of the study; methods of scientific knowledge made it possible to obtain results based on which conclusions were drawn and recommendations were developed to improve the investment attractiveness of the country and investment cooperation between Poland and Ukraine.

Research results

After the start of a full-scale Russian invasion, attracting foreign investment becomes an even more critical and necessary task for Ukraine.

Analyzing the dynamics of foreign direct investment (FDI) inflows into Ukraine from 2002 to 2023 (Fig. 1), there is a positive dynamics of investment activity of foreign investors by 2008 (\$10.913 billion), which became a historical maximum for the entire study period.

The global crisis halved the volume of foreign investment in 2009 (\$4,816 million). In 2010-2012, there was a slight increase in FDI volumes from \$6495 million to \$8401 million. In the period from 2013 to 2015, there was a sharp drop in the volume of investment attraction. Following the Revolution of Dignity in 2014, the outbreak of hostilities in the Donbas, and the annexation of Crimea, the level of foreign direct investment (FDI) dropped to a record low of US\$410 million. In 2015, it reached a negative level of -458 million US dollars. In 2020, due to the negative consequences of COVID-19, FDI in Ukraine was the lowest on record (-\$868 million).

The year 2022 again became a test for foreign investors, who reduced their investments to \$1,152 million due to the war in Ukraine.

According to the National Bank, in 2023, the influx of foreign direct investment (FDI) into Ukraine amounted to \$4,247 million, which is 7.6 times higher than the volume of investments in 2022 but 42% less than in 2021 (Statystyka zovnishnoho sektoru...). However, it is hardly possible to discuss a real resumption of foreign investment. The primary source of capital is the business, which continues to operate

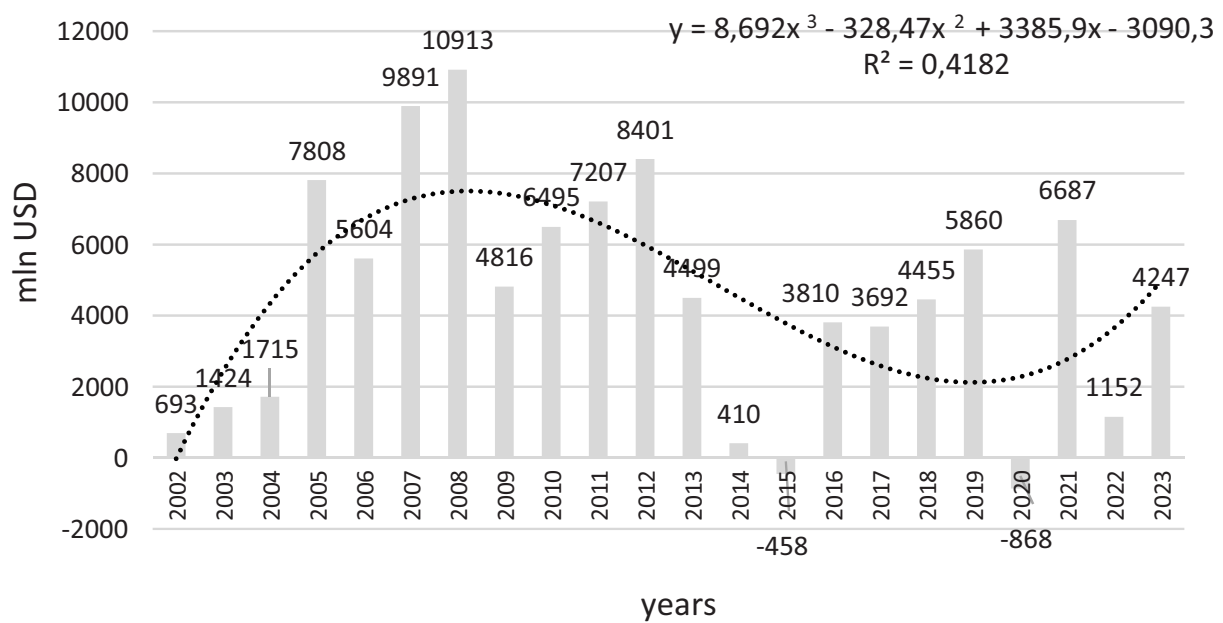


Figure 1. Foreign direct investment in Ukraine for 2002-2023 [mln USD]

Source: compiled by the authors based on: Priami inozemni investytsii (PII) v Ukrainu. Retrieved from: <https://index.minfin.com.ua/ua/economy/fdi/> (access: 08.10.2024).

and reinvest the profits (Savchenko and Stepaniuk, 2024, p. 9). In 2023, the volume of foreign direct investment amounted to \$55.2 billion, which is 6.3% more than in 2022 and 16.5% less than in 2021. According to the National Bank of Ukraine, the volume of foreign direct investment in the Ukrainian economy as of June 1, 2024, amounted to \$2,960 million.

In general, when analyzing the dynamics of FDI in Ukraine, it should be noted that significant adverse events – the outbreak of hostilities in 2014, the coronavirus pandemic, and the beginning of a full-scale invasion paralyzed the country’s economy and led to a significant decrease in the level of FDI receipts. But each time, thanks to the support of foreign partners and government programs to strengthen substantial areas of activity, the state of the economy improved, and with it, there was an increase in the level of FDI inflows to Ukraine (Kovel, 2024).

According to statistical data from the National Bank of Ukraine (Statystyka zovnishnoho sektoru ...) for 2019-2023, the main investor countries include Cyprus (31.6%), the Netherlands (20.8%), Switzerland (4.2%), the United Kingdom of Great Britain and Northern Ireland (4.8%), Germany (4.3%), Austria (3.5%), Luxembourg (2.7%), Poland (2.6%) and France (2.6%), (Fig. 2). Moreover, the overwhelming majority is the return of Ukrainian capital. To a certain extent, this applies to countries such as Cyprus, Luxembourg, the Netherlands, and Great Britain, where some Ukrainian largest holdings are formally registered.

The structure of investments according to the distribution of FDI in Ukraine by sectors of economic activity has not undergone significant changes in 2010-2023. It should be noted that the leading position in terms of interest of foreign investors industry, with a share of more than 30%, followed by agriculture, forestry, and fisheries, with a share of 12.6%, transport, warehousing, postal and courier activities with a share of 12.1% (Fig. 3).

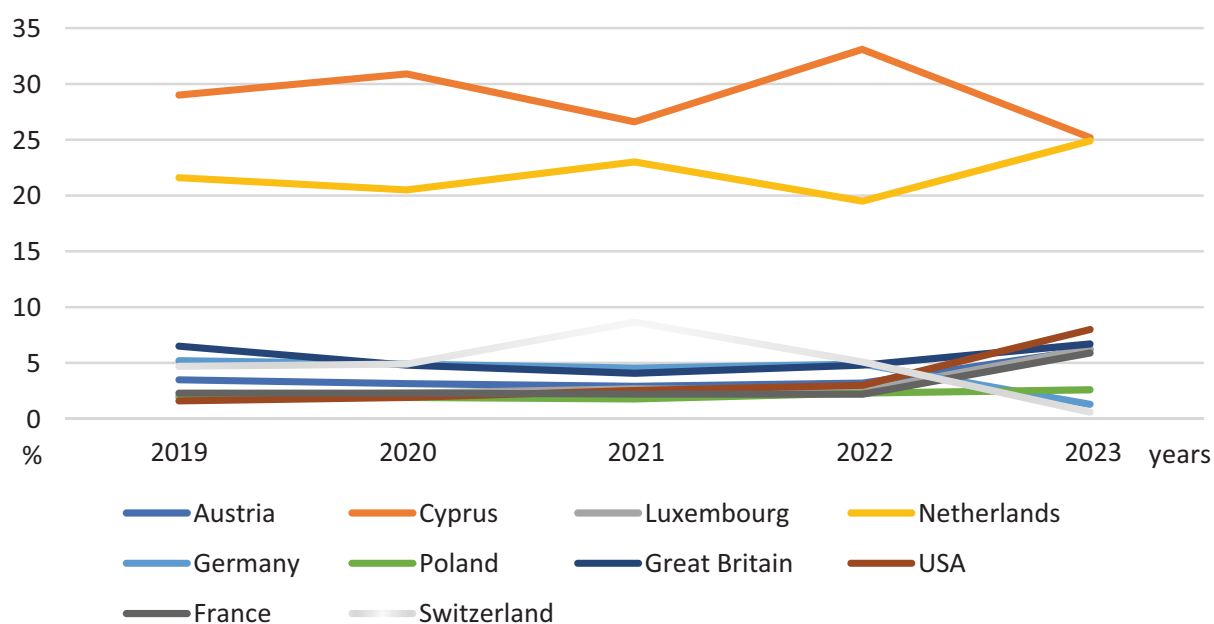


Figure 2. Dynamics of the structure of FDI in Ukraine by country for 2019-2023 [%]
 Source: compiled by the authors based on: Derzhavna sluzhba statystyky Ukrainy (2023).

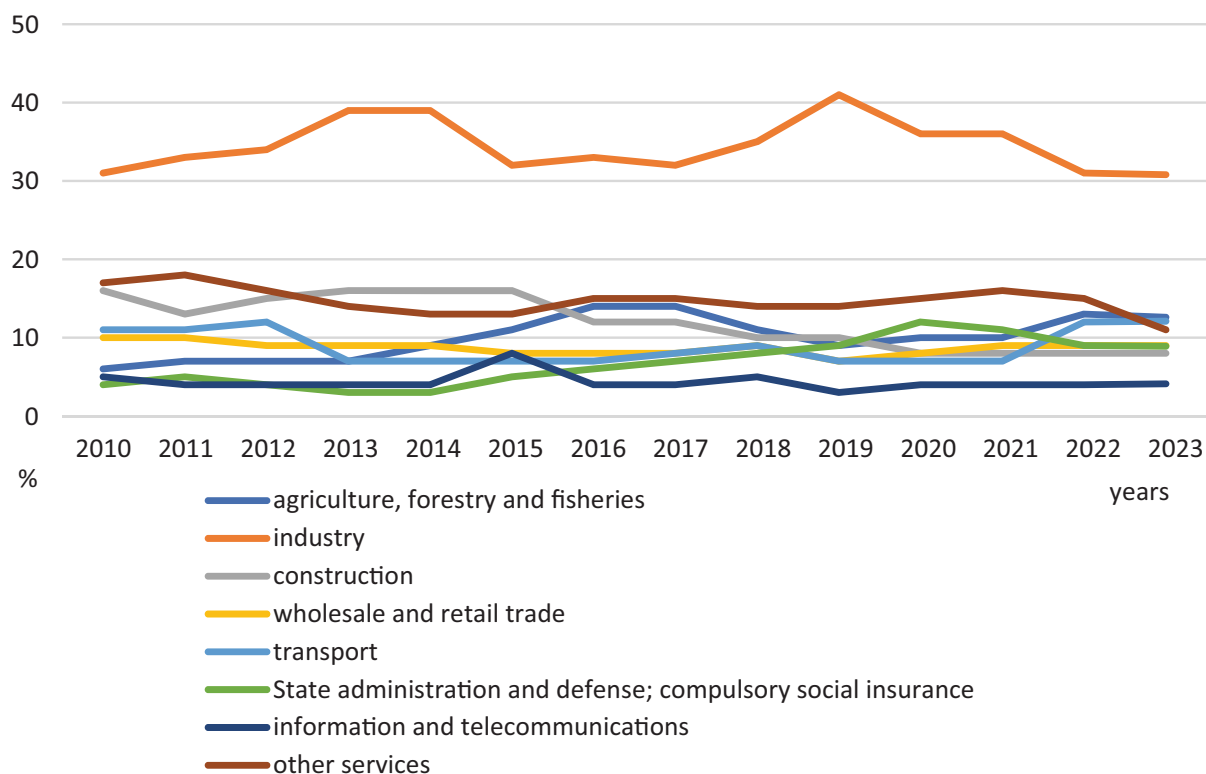


Figure 3. The structure of FDI by types of economic activity
 Source: compiled by the authors based on: Derzhavna sluzhba statystyky Ukrainy (2023).

The decline in foreign direct investment since the start of the invasion of Ukraine does not indicate that foreign capital has completely lost interest in the country. Since 2022, mainly those companies that have already operated on its territory have invested in Ukraine. First of all, this applies to enterprises from the EU countries, the USA and Canada.

For example, in June 2023, the American company Philip Morris International began constructing a new cigarette production plant, which opened in May of the following year. The plant, worth 30 million dollars, was located in the Lviv region. However, the company's second plant, Kharkov, suspended operations for safety reasons. In March 2024, Unilever began building a factory for the production of cosmetic products in Bila Tserkva.

The investment worth 20 million euros is intended to support the development of the company's activities in Ukraine. In March 2023, Bayer announced an investment of 60 million euros in expanding a corn seed production plant in Pochuyki, Zhytomyr region. The project includes the construction of a new seed dryer, the introduction of modern agricultural equipment, and the expansion of storage facilities. The first stage (costing €35 million) of construction was completed in March 2024. In 2023, the Saudi Arabian Agricultural Holding Continental Farmers Group invested 60 million euros, primarily in the expansion of warehouse facilities for storing agricultural products. Among the planned or completed investments, it is also worth mentioning those carried out by companies from Ireland (Kingspan – building materials), Turkey (Onur Group – mining and renewable energy), Germany (Fixit – building materials), and Switzerland (Nestlé – food industry).

Poland is an important strategic partner of Ukraine. At the end of 2023, total Polish investments in Ukraine amounted to \$780 million. It constituted 2.6% of foreign direct investment in the country. Polish investments in Ukraine are mainly concentrated

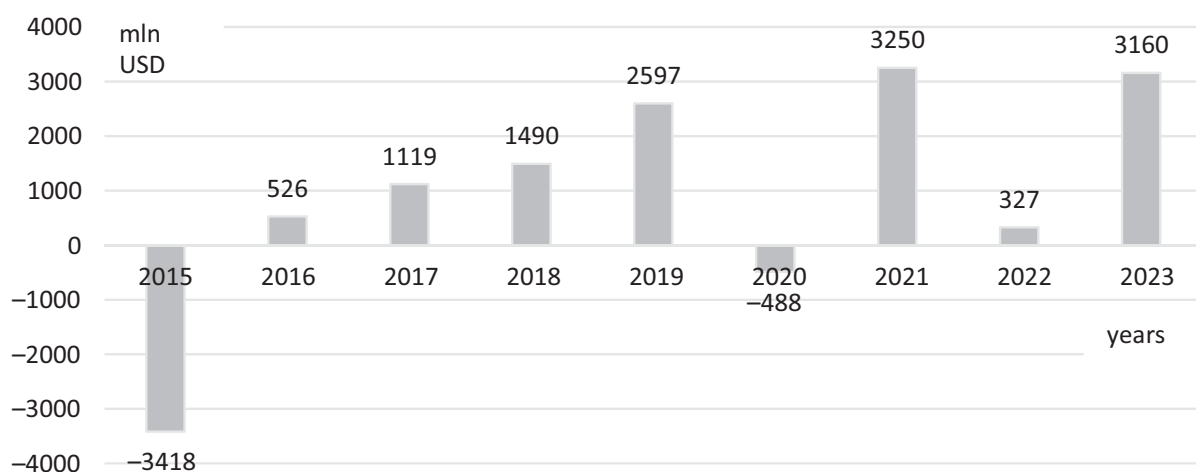


Figure 4. Reinvestment of income in 2015-2023 [mln USD]

Source: Kucherenko (2023).

in three main sectors. The processing industry is of greatest importance, including Cersanit company with a sanitary ceramics factory in Tsviala, Barlinek in Vinnytsia, and the window manufacturer Fakro with a plant in the Lviv region. By the end of 2022, investments in the Ukrainian processing industry amounted to 4.1% of total FDI.

The financial and banking sector also plays a significant role. For example, Kredobank, owned by PKO BP, ranks 14th among the largest banks in Ukraine. In insurance, PZU Ukraine (sixth largest by assets in 2023) and PZU Life Insurance (third-largest company in this field) stand out. By the end of 2022, Polish investments in the financial sector amounted to 5.4% of total FDI. In retail trade, LPP plays an important role, owning Reserved, Cropp, House, and Sinsay brands, which in 2023 formed about 10% of the clothing market in Ukraine. Overall, by the end of 2022, investments with Polish capital in wholesale and retail trade amounted to 2%.

After the start of the war, Polish companies continued investing in Ukraine. In 2023, Cersanit completed the construction of a new production line worth 20 million euros, due to which the plant's capacity will increase by 20%. It was the company's largest activity in Ukraine since the factory's launch in 2007. By the end of 2023, LPP had more than 100 stores there and announced that it would double its presence by the end of 2024, mainly through the Sinsay brand. Despite the attack by kamikaze drones on the Lviv Fakro factory in September 2023, as a result of which the production workshop and warehouse burned down (losses are estimated at 30 million PLN), the company does not plan to leave Ukraine and even intends to build a new production line.

Despite the war in Ukraine, the Polish manufacturing sector has shown significant interest in the Ukrainian market. Polish companies considering investing in Ukraine hope to reduce investment risk through the opportunity to take advantage of loan guarantees from the Ukrainian Facility program (Shevchuk, 2024). This program of financial assistance of the European Union to Ukraine is specially designed to solve the multifaceted challenges that Ukraine faces after the Russian-aggressive war.

Considering the continuation of the war on the territory of Ukraine, the most important thing in the process of forming investment potential is to assess the attractiveness of investing in a certain area as a source of profit on invested capital. The basis for the formation of investment potential is a number of investment advantages of Ukraine that existed even before the war. This list includes favorable geographical location, comparatively lower capital requirements for business placement, adoption of a law to support large foreign investments, simplified legal procedures for doing business, state guarantees of investment security, granting Ukraine candidate status for accession to the EU, abolition of duties and quotas on Ukrainian exports, "transport visa-free" inclusion of Ukrainian logistics routes in the indicative maps of the Trans-European Transport Network (TEN-T). Consequently, Ukraine is now positioned as one of Europe's most promising and competitive countries in terms of investment income (Vibly and Blaut, 2023).

At the same time, the problem of guaranteeing the security of investments during the war and post-war periods cannot be ignored. This aspect is one of the most significant influencing investment potential. Let us highlight several shortcomings that negatively affect investment potential: Russia's war against Ukraine, disruption

of the energy system due to attacks on the Ukrainian facilities, lack of economic transparency in certain sectors to foreign investors, shortcomings in the law enforcement and judicial system, military risks and related threats of destruction or seizure of assets; destroyed infrastructure, logistical difficulties, payment backlogs, as well as the inability to attract foreign loans and insurance.

Conclusions

Ukraine has great potential, including in the field of investment, but it has not yet been fully realized due to military, political, and macroeconomic factors. To resume full-fledged investment, the end of hostilities must first occur. It will be a critical factor in sending a positive signal to foreign investors to become Ukraine's key strategic partners in the recovery process. Ukrainian and foreign organizations have different assessments of the Russian invasion of Ukraine. The estimated cost of reconstruction ranges from 486 billion US dollars (World Bank..., 2024) to 750 billion US dollars, and it is clear that this figure will continue to increase in the world due to the development of war.

Today, world leaders, philanthropists, and famous personalities in the cultural and sports fields actively support Ukraine. Their assurances indicate that Ukraine's restoration will occur with global participation. The key is the victory of Ukraine, the restoration of its territorial integrity and sovereignty, and the further implementation of opportunities for civilized development and modernization of all spheres of the economy and life. However, it is also essential to solve problems that hinder the attraction of investment, such as overcoming corruption and ensuring equal and transparent conditions for doing business, which will increase the investment attractiveness of Ukraine (Dykha, Dykha and Zima, 2022). It is necessary to ensure the fair functioning of the judicial system, which must reach a critical mass of purification, as well as the effective and transparent operation of public authorities. Obsolete practices and opacity should be avoided when allocating public expenditure, while business administration should be as favorably transparent and ensure fair conditions as possible. Trust in Ukraine will be the key to returning human capital and attracting investment into the national economy (Savitska and Fugelo, 2018).

Ukrainian-Polish investment cooperation, which today has prospects for further development, requires significant intensification of efforts in this direction, both for domestic business and in the context of the activities of relevant government institutions and non-governmental organizations, designed to optimize the interaction of economic complexes of Ukraine and Poland and ensure the Ukrainian economy achieves the same positions that Poland strived for on the path of deepening European integration.

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