



Ukraine Briefing
Washington, DC, January 26, 2006

Welcome! My name is Nadia McConnell. I am President of the US-Ukraine Foundation. Welcome to our new offices, I'm glad you could find them. We are delighted to be co-hosting our panel discussion this afternoon on Ukraine's current legal and investment climate, which will be presented by Alex Frishberg and his partner, Alex Schay, of Frishberg & Partners. I would also like to thank Desi Jordanoff, the trade specialist of BISNIS from the Department of Commerce who also assisted us in organizing this event. She will offer a few remarks as well.

I was directed by my development staff to say a few words about the US-Ukraine Foundation for those of you who may not know us. We are actually commemorating our 15th year anniversary of working in Ukraine. We are generally known for our work in what is known as "democracy building." When we first began working in Ukraine, we started at the national level and we had various projects with the Parliament, the Constitutional Court, working with NGOs.

About 10 years ago, we were a little frustrated, which is a word that many are familiar with when thinking about Ukraine, about the pace of reforms at the national level; we turned our attention to the grass-roots level and began a major project, which is working at the city level. We started with 18 cities throughout Ukraine, which we partnered with cities in the United States to work on local government development. Not surprisingly, most picked economic development as their focus area. So most of these cities have done strategic planning, and we are very happy to report that we've seen a lot of progress and success, particularly at the local level in the growth of small and medium-sized businesses in these various cities.

We have 5 training centers located in Kharkiv, Donetsk, Kherson, Cherkasy and Lviv, and I think our latest count is that we've trained over 10,000 local government officials that come to our training centers. We also put out the major publications dealing with local government, one is called "Partners" and the other is called "Aspekty", which is a journal that is more of a "think piece". We have a lot of interest in economic development, obviously, which is important to a successful democracy. So, throughout our work, we have also been interested in cooperating with organizations or entities that are involved in this field.

We've had several conferences, I see Morgan Williams is here and he helped us hold a conference about 5 years ago on Capitol Hill where we talked about the prospects of food processing in Ukraine and the theme was "From the Breadbasket of Europe to Market Basket of the world." We are delighted that we have seen tremendous growth in the [Ukrainian] economy and particularly in the food industry. Currently, some of our key projects include our continuation of the local government projects with the cities; which have taken on several different formats. We are now clustering our cities where they are working on topical issues, again with economic development or communal services as their primary emphasis.

In addition to that, another key project is youth leadership. We started about 4 years ago doing youth leadership programs here in Washington, DC because we wanted to energize some of the youth here and get them involved not only in government, but US-Ukraine relations. Last summer, we worked with the Youth Ministry of Ukraine; we hosted a youth leadership program in Kyiv where we brought together young people from all parts of Ukraine. We are going to continue and hope that there will be two programs this year.

Another project that might be of interest to you is US-Ukraine Policy Dialogue, which we won from a State Department grant two years ago. Through this, we bring together many government representatives, non-government organizations, media, etc. One of the task forces focuses on economics and business in Ukraine and, again, the whole idea of furthering the discussions about the ways Ukraine could and should develop in order to be successful in the economic field. So, perhaps some of you might be interested in working in this area or helping sponsor them. We are a 501(C) (3) and you can visit our website and find ways in which you can participate.

Now, to the main event and our panel discussion. We are very delighted to have Alex Frishberg and Alex Schay. As I look at their bio, they have been in Ukraine also for about 15 years, since 1991. Alex Frishberg has 15 years of experience in assisting Western clients with their Ukrainian transactions. In his tenure, Mr. Frishberg has confronted and dealt with nearly every obstacle facing foreign investors. Mr. Frishberg has published numerous articles regarding Ukrainian commercial legislation and authored the first three editions of Frishberg & Partners' widely acclaimed legal reference guide "Doing Business in Ukraine" (each of you have a copy at your seat). He has also written numerous fiction stories concerning the realities of everyday life in Soviet Ukraine. That must be interesting reading as well!

His partner, Alex Schay, has been with Frishberg & Partners since 1993 and he is actively assisting Western investors with their projects and transactions in Ukraine. After becoming a partner in 2000, Alex has been involved in every direct foreign investment matter that has come to Frishberg & Partners' attention during the course of the past 5 years. For this reason Alex is sometimes referred to as an accurate barometer of foreign investment in Ukraine. Alex has published numerous articles regarding Ukraine's macro-economic and investment climate. He has also spoken at various seminars and investment symposiums in both Europe and the United States.

We welcome them and thank them for sponsoring a reception we will hold after the panel. I also want to once again thank them publicly for their support of our public policy dialogue meeting in Kyiv last November. So, without further ado, I will turn the floor over to Alex Frishberg.

Alex Frishberg: First and foremost, I would like to thank Desi Jordanoff, Nadia McConnell, Markian Bilynsky and Noelle for having us here. The attendance is more than we expected. We came from Kyiv to report about what happened during last year, since the Orange Revolution.

There is no reason to lie. The news is not good. In the last year, Ukraine faced several changes in the government; we went from Yanukovich to a more moderate Yuschenko administration with Yulia Timoshenko. Then, Timoshenko was dismissed as the Prime Minister, and Yekhanurov replaced her. Next, Yekhanurov was dismissed and now we have no Prime Minister at all. Maybe we will have a new Prime Minister after the elections in March, and we don't know who it will be, but it doesn't look good, because it will be either

Timoshenko's block and/or Yanukovich's block in charge. So, basically the same people who were in power one year ago are coming back to power once again. That is because no new people are really allowed to come into power, so the same personalities keep rotating in the government.

Last year, Yushenko was the darling of the Western world. He was carried around like a God by Ukrainian citizens and he even shared valuable time on CNN and in other media during the tsunami. The Orange Revolution was the bright hope of democracy. During the past year, there was a significant opportunity to improve the business climate for foreign investors. But look at the free economic zones. In the free economic zones, the President cancelled all of the benefits and advantages retroactively to January without bothering to announce it well ahead of time. Companies working in free economic zones screamed "bloody murder, we will take you to court!" And rightfully so. All of a sudden, the government changed its mind. It was wrong, Yushenko's team realized, and they decided to give the privileges back. Was this exercise really necessary? Did it give much confidence to foreign investors? No.

And then we had the re-privatization ordeal. 3,000 factories were going up for re-privatization; Yulia Timoshenko really wanted this. Yushenko said "no, maybe 29" to which she responded "yes, you are right, but 3,000 enterprises are slated for re-privatization anyway." This little conflict broke the camel's back and she was fired, but the spirit of re-privatization remains. This ruined the confidence of foreign investors. Eventually, the Yushenko team re-privatized Krivorozhstal. But what did the foreign investors think about this? Answer: large investment is still waiting it out. Again, this was not a good message.

On a smaller scale, if you've been to Kyiv recently, you probably drove by empty construction zones – the "frozen sites". There are literally hundreds of construction projects, 100-150 sites, where people got the required permissions, including land allocation, construction permits, and architectural designs, and hired construction teams and even began excavation. I don't know if you realize how difficult it is to get the necessary construction permissions in Kyiv, but they got them. That is a lot of money invested.

Just as investors/owners begun construction (they even put the concrete pillars in to start the construction), the city froze them. Cancelled. And so these investors now wait. Their money has been invested, and the construction zones are frozen because the city government changed its mind. Fortunately, foreigners weren't allowed anywhere near these investment opportunities. Therefore, for once the foreigners can't complain, otherwise there would surely be a huge scandal on CNN and Financial Times, too. The Ukrainian government is doing this to its own investors. You can imagine the confidence of foreign investors – not great. Objectively, this is the result of the one-year tenure of this President, who was supposed to be better than the rest.

For foreign investors, the question becomes: what is the effect of this mess our business? The result is actually ironic, because the effect is tremendously positive. While the government is in-fighting amongst itself for the positions in the Parliament and the various power sectors, the people on the ground don't get any interference from the government authorities. It is not how it used to be in 1993, 1994, and 1995, when you had to get permissions from tax inspections, visits from fire safety authorities, *sanepidemstantsiya*. Now, they don't exercise any control over companies whatsoever. Is it bad for the government? Probably. Is it good for the business? Absolutely phenomenal. What you have is the purest form of capitalism that you have ever seen in your life. While the nation doesn't have the necessary social

infrastructure underneath it, it is a dream opportunity come true for businessmen.

For small businesses it is a paradise because of generous tax laws. For instance, if your turnover is 200,000 USD per year, you pay only 10% in taxes. That is not a lot. Suddenly, all of these small businesses are mushrooming and they put into their bank accounts during the course of one year not a penny more than 200,000 USD, keeping the rest strictly to themselves. So, despite political upheavals, business is flourishing. In fact, if you look around Kyiv, all of the restaurants, especially the more expensive ones, are filled to capacity with people. These people are not foreigners, as it used to be; they are locals, who have the extra money to spend. Often, more money than the foreigners. Just look at their cars.

Because of Ukrainian taxation laws and the business environment, the local businessmen are at least 45% richer than any of you sitting in this room. They have no mortgages, apartments have been privatized, and everything has been bought for cash. The effect on business? Look at the restaurants and the number of black Mercedes parked in front. It is a shame that government has made itself irrelevant, but the business did not die.

So now that we are talking about the booming businesses on the ground, how is it really done? How do people live? When I visit America, and talk to the people, everyone is under the impression that Ukraine has mafia; that protection payments must be made by the end of the month or people will die. Quite the opposite. Sure, this is how it used to be before President Kuchma came to power in 1994. Kuchma kicked the racketeers out, in sharp contrast to Moscow. If you look at Moscow, for example, they still have Chechen groups, Azerbaijani groups, Georgian groups, Tadjik groups, and they have the Russian "Solntsevskaya Brigada" (Solntsev Brigade) that's supposed to be connected to Mogilevich, but who really knows? These gangs are in Moscow and Saint Petersburg, home to foreign investors; Ukraine does not have any of these types of organized groups. No payments are made at the end of the month, not since 1994-1995.

The real question is how do you do business in Ukraine so that you don't lose? There are risks in everything; all businesses have risk components or variables. It just depends on how you approach them and how you minimize them. For instance, in Ukraine, there are two types of activity that investors generally undertake: import-export or investment. The basic approach is the same so that you don't get ripped off. In import-export, before you sign a contract with your Ukrainian buyer, you want to know who your counterpart is. So investors should perform a background search. Like anywhere else in the world, including D.C., background research can be done on people, companies and, if done on factories, it is called due diligence. You simply send in a team of lawyers and accountants, and they will perform full due diligence reviewing the factory's documentation.

One way to minimize your risks associated with doing business in Ukraine is by beginning with a background research of who your partner really is. Your background research will show you whether your partners have any "connections", and if they do, what type: government, bandit, or none at all. You probably also will want to know whether they have defrauded anybody in the past, their track record, history, their reputation. This information tells you whether you want to deal with your partners at all.

If you wish to proceed, how do you structure the transaction? When you start carrying out your import-export activities, soon enough your business may need a permanent representation in Ukraine. In this case, you may open up a non-commercial representative office with one or two full-time staff members in order to build up your client base. Most

import-export contracts provide for transactions whereby you pay from America in US Dollars to Ukrainian banks, and vice versa. After your operations expand even further, you can open a local resident company, which will be taxed just like any other Ukrainian entity, but is 100% owned by foreigners. Or, maybe, enter into a joint venture with a Ukrainian partner (natural person or legal entity).

If you choose the investment route, not import-export, for example you wish to purchase a factory, once again you would approach lawyers to perform the initial due diligence. We at Frishberg & Partners normally work with Alexander Paskhaver, a famous Ukrainian economist. If you are interested, his materials can be found at www.c-e-d.info.

Mr. Paskhaver assists us in nearly all of our due diligence projects with the accounting component. And we handle the legal component of due diligence for our clients. This is how we would buy-out factories in the beer industry, glasswork industry, etc., and we also clear the Antimonopoly Committee. It all begins with finding out about the factory, about doing your due diligence. If you are involved in purchasing apartments or buildings, again you need to do due diligence. You can easily obtain the necessary documents, including the sale-purchase agreement, the certificate from the Bureau of Technical Inventory and other documents, evidencing title to the investment object. In cases of factories, you must analyze their validity, not only who you are doing business with, but also their debts and obligations, balance book review, etc. This is how you minimize risks in Ukraine by obtaining information.

Once you know what you are doing, you choose your legal form: a representative office, joint venture with a local partner. If so, what form? Equity company? Stock company? Do you want a closed company or offer stock to the public? All of the options are there, just like in America. This is not a problem. If you would like to know more, just look up your topic in our reference guide “Doing Business in Ukraine”, which contains all of the boring details.

Allow me to briefly mention the role of US companies in Ukraine. I don’t know why America is listed as the biggest investor into Ukraine, because in my experience America is the smallest investor. American companies don’t come into Ukraine for various reasons. One of the reasons is that they are afraid. “Mafia!” the press screams, “the sky is falling!” “Ukraine is a volatile nation because the Parliament cannot get its act together!”

For all of the wrong reasons that are not relevant to Ukraine, American companies are scared. Therefore, they tend to stay in their own backyard, facing stifling competition amongst themselves. Meanwhile, their competition from Europe is already flourishing, not just in Kyiv, but throughout Ukraine. If you don’t know this fact, then simply do a “Google” search over the Internet. You will see that your competition is already well ahead of you in Ukraine. They solve their problems easily because the problems are not really all that great.

Another reason American companies don’t invest in Ukraine is that their corporate decisions are such that they come in via European companies. For instance, Coca Cola Amatil comes from Australia, they don’t come from America. General Electric comes from England, not from America. McDonalds is from Austria, I believe. So, a lot of times companies don’t come from America, yet they are attributed to American investment in Ukraine. That’s why I believe there is very little actual American investment. At the same time, I will stress again that American companies’ competitors are already there, and for quite a while. And, somehow they beat the odds.

So what are the real risks they assumed? Mafia? No. Weak court system? Definitely, that is a risk. With respect to your contracts, for example, what if you must go to court? And then someone comes to the judge and influences the judge? Unfortunately, that happens all the time. There are two distinct ways to influence a judge: give them money or make a phone call. Either way, the courts are weak and you often have bribes going against you, if you have unscrupulous competitors.

I'll quickly summarize my feelings about Ukraine's immediate future, as I wrap up my speech, in light of the upcoming Parliamentary elections. Everyone who has lived in Kyiv since 1991 pretty much knows all of the political figures, because no new people are allowed in – only the old guard is in the government. Ukraine does not have the Kennedy School of Government, which brings up new leaders with ethical standards for today's transparent economic world.

For instance, the upcoming Parliamentary elections – who is going to go against the “new incumbents”? These people have their own seats in the Parliament. They have Mercedes. More, they have money, millions of dollars for the next election campaign. Some have the ability to rig the votes. They also have people with baseball bats to knock the knees out from under the competition. An average person on the street simply does not have those three political tools at their disposal. How can an honest person become a member of the Parliament? They cannot. As a result, there are no new people in the government over the last 14-15 years. Who will come out victorious from the March elections? It simply makes no difference. All of these politicians are the same.

The disconnected gap between the government and the people after the Orange Revolution is tremendous. A year ago people had the illusion that a change in the government would alter things, that miraculously there would be no more corruption after the Orange Revolution. The people now realize that it was merely an illusion. Their hopes were so high, and they have now fallen so low, that now there is a nation of non-believers. When they vote, they will not vote for somebody, but against the other party. They don't listen to what television says anymore. As a result, nobody wants to pay taxes and yet the business goes on. More, it prospers, and the government doesn't interfere. They are busy fighting amongst themselves.

In conclusion, on a positive note I can honestly say that psychologically Ukraine has already become much more Westernized than anyone could have imagined. It no longer has a Soviet mentality, and thankfully it does not have a Russian mentality. It has a Western European mentality: Ukraine is entrepreneurial, it is vital. It is pure, capitalistic style business. This type of mentality in business on the ground will continue to grow and develop with or without American investment coming in. The question is: do you really want to miss the train when your competitors are getting on board? Thank you.

Alex Schay: Ukraine may be viewed as an exotic market, but – like it or not – it is the fastest growing economy in Europe. The Russians figured this out in 2001-2002. Russian businesses make money anytime oil sells for over \$14 per barrel. You can sink islands with that sort of liquidity. They began to take an interest in specific areas of the Ukrainian economy. And, as my partner Alex Frishberg suggested, Europeans entered the market shortly thereafter. So, if they figured that out, it is time for us to take an “anniversary assessment” and to examine some of the things that are attracting investors to Ukraine as well as some of the issues that dissuade people from coming to Ukraine and, finally, to analyze some of the opportunities that are waiting for you in Ukraine should you decide to have that sort of adventure.

First of all, in 2004, Ukraine had absolutely astounding growth. A GDP growth of between 10-12%, depending on who you ask. Obviously, some of that can be attributed to the “de-shadowfication effect” inasmuch as tax rates were going down and more businesses were being officially declared. Thus, you had business that was going on beforehand that was never officially declared (registered with the Ministry of Statistics) suddenly being registered. So, perhaps the GDP growth rate was not 10-12%, but more like 7-8%. That still puts Ukraine in the top tier of growth worldwide, and at the very top of the heap as far as Europe is concerned. That growth fell somewhat in 2005, largely due to spending and other intricacies associated with election-year politics. It fell to something like 3-4% per annum, which is still respectable.

If you look to the future, most experts agree that from 2006 until 2010 Ukraine’s economic growth will be on average 5-6% per year. At the same time, if you have these growth levels, you have opportunities for a tremendous return on investment. A relatively safe investment, for example, would be corporate bonds, which account for roughly 47% of the Ukrainian securities market (both stocks and bonds). On the conservative end, are blue-chip bonds, such as those issued by Ukrtelecom and the steel and mining industry, etc. Such bonds typically yield a 12-13% return on investment. Riskier corporate bonds, on the other hand, can return between 16% and 17%.

When I talk about clients, and I see all of the new projects that come across our doorstep, the average return on investment that they are looking for, if they are going to take an equity position in a Ukrainian company, is between 20-30%, sometimes more. Real estate is an area that, despite the 1998 ruble crisis which impacted Ukraine as well, has been growing. At this point, prices for real estate in Kiev are growing by 5% per month. And, if you take a look at Ukraine as a whole, real estate is increasing in value on average between 30-40% per year.

There are some intricacies related to such real estate growth. Specifically, there are three basic groups that are in a position to sign off on any kind of a real estate project, whether it is office buildings or residential construction. And these groups are (i) banks, (ii) construction companies and (iii) government. The banks provide the financing (in some cases the construction companies as well), and the construction companies certainly provide the know-how and the connections. The government, however, is the one that provides the certificate of exploitation. So, the release of new property that is ready for use (i.e., people can live there) may be regulated in order to keep those real estate returns artificially high. At any rate, we hear plenty of stories about government delays in issuance of so-called Certificates of Exploitation as one of the reasons for artificially-inflated, real estate prices.

What about the stock market? It is still very thin, and you hear a lot of complaints, especially from insurance companies. They don’t know what to do with all of their premiums. Where do you put them? Typically, insurance companies use securities as a way to get a return on investment on their premiums. This noted, in 2005, the Ukrainian stock market nearly doubled in size; it grew by 1.9 times. That notwithstanding, the Ukrainian market is still a very illiquid, bond-driven market. In 2005, equity returns, however, stood at about 35%. And, a 35% increase in the market for equity securities compares very favorably with anywhere else in the world.

So, where does that leave you in terms of the sectors represented on the Ukrainian stock market? The usual suspects: metallurgy, mining, energy, telecoms, and chemicals, in that order. Furthermore, one should note the recent development of investment funds in which anyone can take part if they know where to look. Most experts agree that Kinto Investments

and Securities sets the market standard, and they have numerous funds. On their equity funds, you can expect to receive 100% return on investment each year. If the fund contains a mixed basket of bonds and equity, you can expect to receive a return of 50-70% per year. And, in that case, your risk has been somewhat mitigated. KINTO's bond funds offer 15-17% return on investment. KINTO's real estate fund offers approximately a 40% return on investment; truly a remarkable return.

What are some of the positive developments we can look to one year later in terms of new developments that directly impact foreign investment? As Alex Frishberg suggests, such positive developments are, unfortunately, very few. That said, there were significant reductions to import duties and customs tariffs that were introduced in March 2005.

Essentially, the US government told Ukraine: "listen, we helped you both financially and morally with the elections, so WTO accession is a priority for us, will you please reduce your tariffs." I went to one of our clients, Jahn General Products (who gave us permission to use their name – they are one of the largest Scandinavian importers of fresh food products), and I asked Fleming Jahn "so, these new tariff reductions, how have they impacted your business?" He responded: "Until March 2005, tariffs and customs duties accounted for 40-50% of the total value of our products. In April to May of 2005, they only account for 10-15% of the value of our imported goods." A very significant reduction.

There has also been relaxation, a sort of state of managed anarchy if you will, of the system associated with the procurement of approvals or permissions. For example, if you are running a software-development facility and you want to employ your programmers as subjects of entrepreneurial activity to get around the 37.5% employment taxes, there used to be a fairly stringent procedure you were required to undergo in order to register as a subject of entrepreneurial activity. Now, you submit the documents, you wait fifteen days – whether you are approved or not is irrelevant – if you've filled out the application and submitted the proper documents and you've allowed the required amount of time to expire, then in fact you have already made a good-faith effort and the application is complete. The same can be said of the infamous Rule No. 2.8 of the fire safety code. How many horror stories have you heard about that? The same situation applies, you've submitted the documents and you wait the required amount of days and you will receive automatic approval. These sorts of reductions in red tape certainly are positive developments for business in general, and for foreign investors in particular.

During the past year, the Yushenko Administration has also made an effort to ease the difficulties associated with procurement by non-residents of Ukraine of non-resident work permits (such permits are needed if, for example, a foreigner wishes to work for a company as its Director). The unofficial aspects of that application process have been completely removed. You submit the application and documents, wait the required time, pay the 175 Hryvnia official fee (approximately 35 Dollars) and you should get the work permit.

Sadly, this ends the list of positive reforms, and we enter into negative territory. For example, over the course of the last year, there was a lot of talk about reducing value added tax from 20% to 15% in two stages. It never happened. I was talking about this in The Netherlands in April of 2005 – it never materialized. Same conversation with respect to the reduction of corporate profit tax from 25% to 20%. And, at the same time, if we didn't see these positive developments taking place, you had the unannounced and retroactive removal of the ability of a foreign investor to make an in-kind contribution to the charter fund of their resident company and avoid VAT. This effectively introduced an overnight, unannounced 20% new

tax on foreign investment. When asked to explain, the Ukrainian government gave a logical explanation. They said: “We want an even playing field. If Ukrainians, who are buying the same equipment, need to pay 20% VAT when setting up their companies, why should foreigners have a 20% advantage?” The argument makes sense, but it was not explained in advance, and this did not make foreign investors feel secure with respect to Ukraine.

The same can be said about the removal of free economic zones. Most of the work that was being done by foreigners was completely legitimate and, in many cases, the foreigners set up their operations in such free economic zones specifically to achieve their tax benefits. The government removed these benefits overnight, and when asked to explain, it responded: “Oh, money laundering, havens for corruption.”

Then there has been this sort of ambiance of mistrust associated with the concept of re-privatization. Ultimately, as Alex Frishberg suggested, re-privatization only affected one or, perhaps, two factories. Anytime you start to talk about amending previously-established ownership rights, it sends a shudder of fear throughout the serious investment community.

What sort of opportunities are there? We’ve looked at the overall environment, we’ve looked at the pros of the Orange Revolution and we’ve looked at the cons as well. What sort of opportunities attract investors to Ukraine? The biggest opportunity is clearly the fact that if you don’t get there, your competition will, and you will miss out on establishing yourself on the market by 1,2,3 to 5 years. Still others come to the market to take advantage of incredible growth in real estate prices. But there is one area, a sort of unsung reason why foreign investors establish themselves in Ukraine, and that is to reduce their worldwide costs of production. We saw it first with IKEA and then in the automotive industry and later on in the manufacturing of electronic components, wood processing, clothing, textiles, etc. Essentially, if you can bring in your materials, which are under one product classification, into Ukraine, you process them in Ukraine and get them out within 90 days, change the product classification code of the materials and, finally, if you don’t exceed the original value of the goods by 5 times or more, you avoid all import duties and all customs tariffs. Most of these “production outsourcing facilities” are established in Western Ukraine, which is very close to Europe and extremely depressed so that the costs of labor and production are very low.

You see the same thing happening with offshore software development facilities, but those are based around the technological centers – in Kiev, Kharkov, Dnepropetrovsk, etc. Again, it increases your bottom line in the West. You don’t make money in Ukraine, but you increase your Western profit margin.

There are various reasons why people come to Ukraine. To compete with competition, to establish their presence, to pursue a strategic relationship, or to cut their bottom line or increase their profit margin in the West. No matter what the reason, the bottom line remains the same: the early bird gets the cheapest worm. Thank you.

Desi Jordanoff: I will be very brief because I want to leave the audience time to ask questions and we’re ready for a lot of important ones.

I am Desi Jordanoff, I am with Business Information Service for the Newly Independent States, US and Foreign Commercial Service at the U.S. Department of Commerce. I would like to thank John Kuhn, Nadia, Noelle, Vira, Ulyana and all the colleagues from the US-Ukraine Foundation for hosting today’s event. I would like to thank Alex Schay and Alex

Frishberg of Frishberg & Partners for sponsoring the event and everyone that is here today, our clients who perhaps got our announcement and other businessmen, experts and officials.

We have gone over how US companies invest in Eurasia (Russia and the independent states). Particularly, I cover Ukraine and several other specialists in Washington, DC cover other countries. We also cover different industries in our portfolios. I am fascinated with Ukraine and I handle that portfolio with a great attention and energy. I just wanted to mention a couple of programs that we offer to our clients. Trades and Tenders are requests for assistance in obtaining US products and services and Search for Partners, a program that emphasizes long-term partnerships and investment projects. The Ukrainian companies send their requests to our representative in Kiev and/or contact us in Washington, DC. We receive many requests from Ukrainian companies that are interested in working with US companies. The requests vary between export or investment in projects and industries across the board. (Real estate, construction, infrastructure or other mentioned industries). We are here to help. We have 15 representatives overseas and we send them out to clients and to other interested companies and organizations. Our representatives counsel companies with the objective to bring our efforts to success and to close the deal. We do not get involved in negotiations, and do not charge clients for our services. We are here to help our companies succeed.

Our website is www.bisnis.doc.gov. We constantly update it with new information and it currently is in the process of being updated. I don't want to bore you further, I just want to mention a couple of things about how precisely our colleagues from Frishberg & Partners evaluated the situation in Ukraine. I thank you for being objective and presenting the reality without additional coloring. Now, I will leave room for questions. Thank you.

Q & A Session:

In the last 6 to 12 months, what kinds of US investors have come to Ukraine and in what industries?

Desi: From our experience, we see a lot of progress in the construction industry. There are combinations of either real estate/other commercial construction projects. When I was there (in Ukraine in the Fall of 2004) there was quite an interest generated in construction with US technologies. In that area, US construction companies were involved in projects in building commercial and residential real estate. Currently the construction industry in Ukraine is developing in the direction of new technologies, modular building, but there still is combination of construction of high rises with panels and modular building. The companies are trying to capitalize on their knowledge and the existing technologies with incorporating the innovative technologies of building high-rises. The companies are starting to move in the direction of much faster and low-cost construction.

The other industry, which is very tricky as to how we, as government entities approach it – Food production and agriculture. Currently Ukraine is trying to re-structure the industry. In this industry we get many requests for agricultural equipment and technologies.

The environmental field is very promising and presents with big opportunities, specifically in reference to innovative technologies, such as recycling and converting waste, (water and sewer waste, for example). Currently I am working on a substantial project, which I hope will be very successful. The project is for exporting US equipment for water waste conversion into energy (a US company owns the technology and has the equipment that is very

innovative and leading in the world in the field of water waste conversion).

There are a couple of other projects, for example in the Consumer Goods industry, but the competition from the companies in Western Europe is quite stiff. We still have some new projects that we have assisted with depending on the demand from the Ukrainian companies. The best feature of our program is that we answer inquiries that are a result of customer demand.

Question about water waste into energy equipment.

Desi: Apparently, this equipment is working to clean and convert the water waste and water sewer systems. The way it works is, (I am not an engineer and I cannot expand on this) that the equipment not only is clearing out waste and transporting it out, but also is using the waste to get energy which will be used in industrial production. There are further opportunities to convert it into electric energy. I am not a specialist, but these are the basics. The technology uses water and sewer waste and after a specific processing delivers a product, which is energy. This is a very innovative technology.

Question: If government is ignoring business, yet if you are in the business it is highly regulated, how do you see that going?

Alex Frishberg: If you have projects, for instance energy, which require government assistance and regulation, then you have to work with them. You have no choice. How do you work with them in such a way that they want to cooperate? You need establish personal relationships. A lot of people, especially Russian companies, do it on the basis of an envelope. It depends on what is in the envelope, but that is how you get your cooperation. That seems to work for Russian companies well. However, we just try to arrange this on the basis of a phone call that keeps the doors open and we get some type of acknowledgement that they have to work with us because the supervisory authorities are watching over them.

Desi: If I may add? When we have a procurement tender that comes from a Ministry in a country and we work to push through and have American companies bid in an equal manner. We do have an organization in the Department of Commerce, called Advocacy Center. The specialists from the Center typically negotiate to level the playing field so that American companies have an equal opportunity to bid in a tender. In some places, the guidelines of the tender or the rules specified by the government of the country announcing the tender are so confusing and designed to not allow certain companies to enter the bid. This makes it simply impossible to work through. So, one way is through good relationships, but the other way is to use our government programs and specialists that are willing to work on that level to negotiate with governments. It is a tough job, but our colleagues' objective is to level the playing field for US companies.

Question: We had a government with Kuchma, then we had a promising government with Yuschenko, and now it is sort of coming back and we will have another new government. What is going to happen in March after the elections? What happens to the "good relationships"?

Alex Frishberg: This happens every time there is a shift in the government. Every time

someone leaves there is the concern about who will be in place in another two or three weeks. A month later you find out that it is a different person in the same government. Once the dust settles, once you know who is in position, you do the very same thing again. You call your friends, you ask the secretary to connect you, you bring their secretary a box of candy, and you become a new best friend for life. You must let the dust settle each time. If you have a project, then wait until the middle of May when everyone comes back from May-Day holidays, recovered from hangovers.

Question: What about the automotive industry? What is happening in that market?

Desi: I'm not a specialist that covers this industry, there is another colleague in BISNIS, a Trade Specialist that covers the automotive industry. I do know, however, that this industry is quite developed and there is quite a lot of foreign representation and competition. There is a lot of interest in establishing plants that are supplemental to the automobile building industry. In other words, companies that have already set automobile production or assembly facilities are looking to partner up with other US companies that will supply the automotive components and spare parts. This is pretty much the trend, to establish facilities for automobile assembly and for production of supplementary products, such as components, spare parts, all types of injection moldings, etc.

Question: I actually wanted to add when you were talking about production outsourcing. One opinion that I heard is that going into the West markets using production outsourcing in Ukraine doesn't have the competitive advantages required to compete with countries like Bolivia, and I just wanted your opinion on this and on the competitiveness of Ukraine as a country for production outsourcing. How long will it last?

Alex Schay: Well, you may have a point, in terms of geographic proximity and taking into account the free trade agreement with America that's foreseen. Most of the production outsourcing that we have seen, especially in the textile and clothing industry, comes out of Belgium and out of Denmark where there is geographic proximity. Where we really see the advantage is in the production outsourcing sector is with respect to more high-tech items where you deal with an educated workforce of people who were, perhaps, better trained in engineering fields. So, again, you are talking more about electronic components, automotive components and things of that nature.

Desi: May I add something to this? The geographic proximity also plays a role in the consumer goods industry (apparel and footwear category and textiles). This is one of the most saturated and competitive industries that we can look at particularly in Europe. And when it comes to European goods, and not only European goods, but the cheaper products from China and Turkey that are flooding the region, there is a particular consumer behavior in regard to the requirements of how apparel should look in terms of fashion. However, in terms of fabric and accessories used in production of apparel there is a high consumer demand for quality. As far as the competitiveness in this area, US producers are not very competitive, because of the traditional consumer preference for European Fashion. In addition there is price effectiveness and price competition in this segment as well. I don't know whether your question was the other way around as to how a Ukrainian company would compete in the market.

Question regarding exports from Ukraine to the United States.

Desi: This is in a sense the thin line in regard to where the good is coming from. We don't promote imports to the US, but imports are not always bad for the economy. Typically for the American market: this is a huge market that is saturated with products lower in cost coming from all parts of the world. Competition is quite stiff and in order to establish a Ukrainian brand on the US market there should be a thorough research about what segment to target and how to structure the price.

Nadia McConnell: Thank you very much. I think we got a very candid picture, but also one that invites you to not be doubters and come to Ukraine. Thank you all very much for attending and please enjoy our wonderful reception hosted by Frishberg & Partners.