

*Considering the nation's growth rate, European producers would be foolish not to pursue advance in this direction. Professional Parquet tells you how to go about it.*

## Ukraine, big opportunity?

Ukraine and Russia are two areas with extremely rapid growth at the moment. Although European producers would be foolish not to take advantage, there are a few problems involved. The idea of "going it alone" as a foreign company without government assistance by relying solely on local operators or those in other nations nearby is equally unadvisable. These are various reasons, and all can be traced to the recent international opening

of these countries to the democratic process, which still remains uncertain, however.

These high rates of development have not yet been transformed into corresponding levels of wellbeing for most of the population, and conflict is high at both the social and legal levels. We observe promising markets on one hand, but if we cannot go there alone, then what must we do? The most intelligent solution is to find a European partner, Polish, for example, and then open productive and commercial units in joint venture.

The decision to find a commercial partner with which to begin operations in nations like Ukraine helps avoid the extremely unpleasant phenomenon of "raiding" in which the minority shareholder - usually a local - first accepts the foreign capital offered and then a few years later, without any agreement or warning at all - takes complete control of the company and chases the foreign investor away even before foreign capital has completed the cycle originally foreseen for its return... Ukraine is this, too!

### Europeans: the great opportunity

The 2012 European Football Cup will be jointly hosted by Poland and Ukraine, who will build the fa-





cilities required for the event not yet present. This means hotels, roads, and offices - and therefore parquet and ceramic tile floors - and everything else necessary for modern organization.

Who's going to foot the bill? The choices made by the Polish government will have a big effect in Ukraine as well because - and it's well worth noting - there is not direct relationship and for which reason the Poles will pay for the Ukrainian infrastructures, but only in terms of co-ordination, because Poland is a EU nation, Ukraine no. Its therefore easy to imagine that works associated with a Polish development plan that affect soccer championship play in the two nations may be the object of joint study and completion by Italians, Poles, and Ukrainians.

We recall a phrase already highlighted in the Poland Dossier by a Polish Commercial functionary in Rome: *"In 2007-2013, Poland will be the greatest structural fund beneficiary in Europe. Almost 92 billion Euros will be made available... In order to benefit from such structural funds, Italian companies should set up their own companies in Poland. Funding for projects involving the purchase and renovation/restructuring of Polish companies acquired 100% alone or through joint venture, and therefore the acquisition of new machinery and technological lines can be obtained"*.

These structural funds from which Poland will benefit can be used to finance the works for the 2012 European Football Cup only wherever the infrastructures involved (roads,

highways, airports, etc.) coincide with those required also for the Cup to be financed with the funds set aside by the Polish government and the participating foreign investors.

This access to European funds does not hold true for Ukraine because it is not a part of the European Union. The nation probably intends to finance the infrastructural works required by using internal funding or seeking foreign capital.

## Currency

In 1992, Ukraine introduced a temporary currency, the Karbovanet, with the immediate result of no longer being a member of the former Soviet Union's Ruble area. In 1996, the Hrivna (UAH) definitely replaced the Karbovanet, and the law established that the UAH is the only currency acceptable for exchange between residents in Ukrainian territory.

In recent months, the UAH/US Dollar exchange rate was 4.85 UAH per 1 USD. As regards the Euro, the Ukrainian currency oscillates with the Euro/Dollar exchange rate, and at the moment is 7.49 UAH/Euro (June 2008). Foreign currencies cannot usually be used in Ukraine to liquidate monetary obligations, with the exception of international transactions, foreign investments, and international trade. Payments between residents in Ukrainian territory made in foreign currency are prohibited, including the payment of salaries by Ukrainian companies. This rule does not apply to the borrowing or repayment of bank

## FREE TRADE ZONES

*The benefits previously granted to free trade zones were eliminated by the previous government and the current administration doesn't consider their restoration to be a priority. Although companies operating in these zones still enjoy benefits granted previously, nothing in the future can be certain. Today's areas can be divided into three categories:*

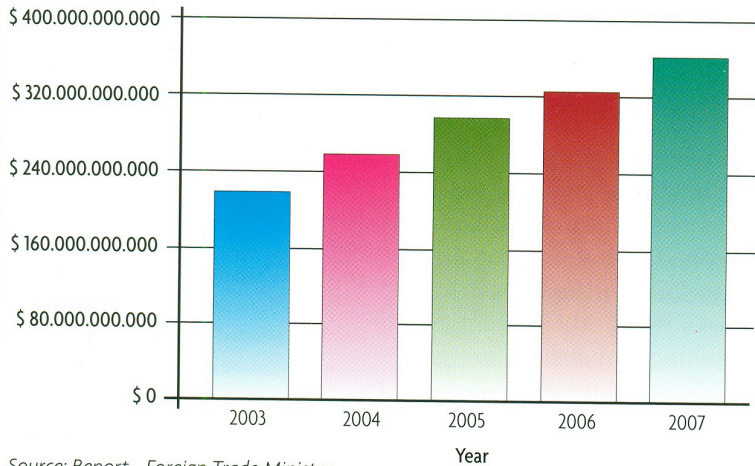
- special economic zones;
- territories with special investment programs;
- territories in which economic development is given top priority.

*These zones and territories are subjected to different taxation, and each has its own respective administrative authority. The special economic zones are usually created only for a determined period of time (from 10 to 30 years). The key elements can be summarized as below:*

- the company is exempted from paying taxes for the first 3 or 5 years required to get the business up and running and then subjected to facilitated taxation for the following years;
- exemption from paying Customs duties and VAT on imports;
- reduced withholding tax brackets on the dividends and income due to non-residents;
- exemption from the obligation to convert income obtained from foreign currency into local currency;
- exemption from obligatory social security contributions and taxes on landed property or reduced tax brackets as an alternative.



## GROSS NATIONAL PRODUCT (GNP)



Source: Report - Foreign Trade Ministry

loans in foreign currency.

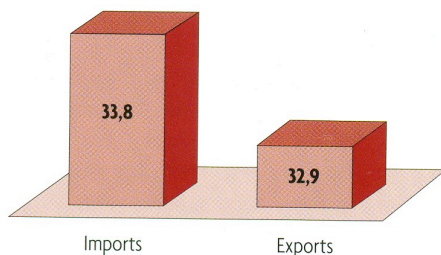
### Economy

Growth in the GNP in 2007 amounted to 10.7%, a marked upswing over 2006, and this was accounted for by both a rise of 11% in industrial production and inflation (around 5% in 2007 compared to the 2.6% in 2006) with an 8% unemployment rate.

A few words about the GNP: pro capita income in Italy is around 17,000 Dollars, in the USA, around 42,000, in China around 7,700 and in Ukraine around 7,800 (2007).

Inflation is not calculated by international standards but rather by a list of local products which in Ukraine is over-estimated by the presence of agricultural products (60%) at the expense of energy and real estate costs. Whenever the inflation index could be corrected with these data, its real value would have been 10% at the end of 2007 and

### EXPORT DYNAMICS COMPARISON BETWEEN 2006 AND 2007



Source: Report - Foreign Trade Ministry

12% in the first quarter of 2008. Driving the economy are the iron, carbon steel, and chemical sectors, and these have triggered a 30% jump in domestic consumption and a 40% increase in requests for bank credit in just the last year.

Also note that the woodworking sector recorded a +13.9% increase, whereas machinery manufacturing rose by 23.3%.

Foreign exchange is fairly lively with 25.4% of the nation's exports going to Russia, followed by Turkey with 7.2%, Italy 6.6% and Germany and Poland 3.5%.

This classification above changes drastically when the subject is imports, however. Russia is still at the top and responsible for 28.5% of Ukraine's imports, and is followed by Turkmenistan with 10.2%, Germany with 9.1%, China with 4.9%, Poland, Kazakhstan, and then in 7th place, Italy, with a mere 2.8%.

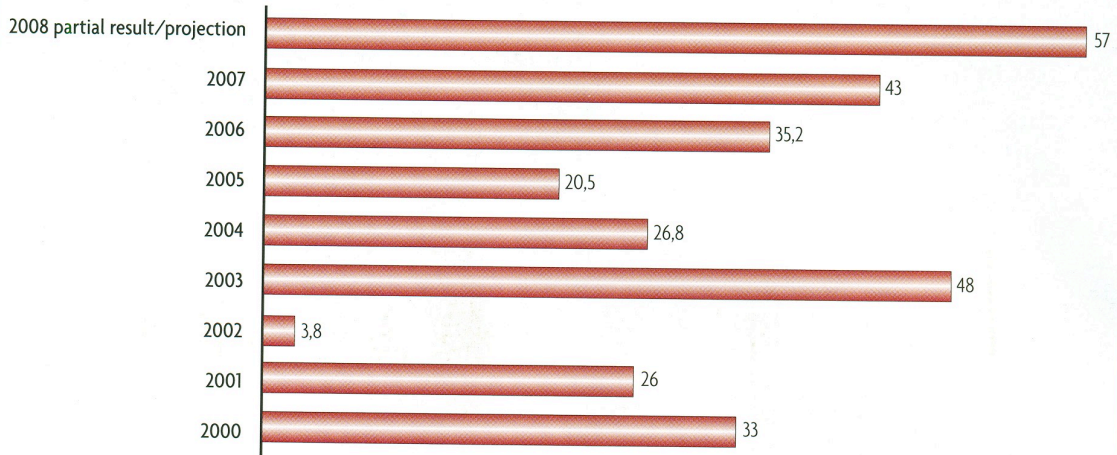
### Tax relief and benefits

Current company taxation legislation no longer contemplates a period of so-called tax holiday (the initial period immediately following a company's incorporation in which taxes and duties are not charged) or any other types of tax break in favor of foreign investors. The previously existing five-year tax holiday for foreign investors has been definitively abrogated and is no longer used, with the sole exception of investments in the automobile industry in which the total amount is equal or superior to 150 million US Dollars.

That being said, investors are subject to the same taxes as local



### INCREASE OF ITALIAN EXPORTS TO UKRAINE - DATA IN PERCENTAGE OF GROWTH OVER PREVIOUS YEAR



Source: Report - Foreign Trade Ministry

operators are, with the exception of certain tax benefits, such as the possibility to import goods destined to be contributed in capital account for the foundation of a Ukrainian company without paying Customs duties. In order to qualify for this benefit, the importer must issue a guarantee equal to the amount of the Customs duties normally due on the goods with a maximum 15 day enforcement term to the favor of the Ukrainian Revenue Office. Such guarantee will be discharged when the asset is duly registered in the company's balance sheet. Furthermore, a company is obliged to pay import duties whenever the goods contributed in capital account are sold within three years from the date of registration of the investment.

The importation of capital goods is VAT-exempt whenever they are contributed in capital account for the founding of a company under Ukrainian law. This exemption from VAT and Customs duties is

applied only if the asset is not classified under those subject to such tax. In the event that these goods contributed in capital account are sold within three years of the date of the investment's registration, both the VAT and the respective Customs duties must be paid.

As of 01.04.2005, investments are no longer exempt from paying VAT.

### A word with Ukrainian operators...

The Ukrainian floor laying company that we interviewed is known as Lisgal (lisgal@lviv.farlep.net), a Swiss-Ukrainian joint venture set up in 2000. We spoke with Mr. Zavarenski Michaelo Marianovich.

*For how many years have you been working in the market and how many people visit your showroom?*

We've been working for 8 years, open to the public from 8 in the morning until 6 in the evening. Every day, an average 6-8 people visit our showroom.



**PRODUCTION OF PARQUET IN UKRAINE (M<sup>2</sup>)**

	2006	2007
Mosaic	1,980,000	2,030,000
Solid wood 6/13 mm	270,000	300,000
Solid wood 14/23 mm	2,930,000	3,090,000
Layered	6,700,000	7,200,000
<b>TOTAL</b>	<b>11,880,000</b>	<b>12,620,000</b>

Source: developed by the author after interviews with operators in the Ukrainian sector

**IMPORTS OF PARQUET INTO UKRAINE (M<sup>2</sup>)**

	2006	2007
Mosaic	90,000	100,000
Solid wood 6/13 mm	20,000	40,000
Solid wood 14/23 mm	100,000	90,000
Layered	180,000	200,000
<b>TOTAL</b>	<b>390,000</b>	<b>430,000</b>

Source: developed by the author after interviews with operators in the Ukrainian sector

**DOMESTIC CONSUMPTION OF PARQUET IN UKRAINE (M<sup>2</sup>)**

	2006	2007
Mosaic	850,000	930,000
Solid wood 6/13 mm	85,000	180,000
Solid wood 14/23 mm	1,300,000	1,480,000
Layered	1,580,000	1,400,000
<b>TOTAL</b>	<b>3,815,000</b>	<b>3,990,000</b>

Source: developed by the author after interviews with operators in the Ukrainian sector

**EXPORTS OF UKRAINIAN PARQUET AROUND THE WORLD (M<sup>2</sup>)**

	2006	2007
Mosaic	1,220,000	1,200,000
Solid wood 6/13 mm	205,000	160,000
Solid wood 14/23 mm	1,730,000	1,700,000
Layered	5,300,000	6,000,000
<b>TOTAL</b>	<b>8,455,000</b>	<b>9,060,000</b>

Source: developed by the author after interviews with operators in the Ukrainian sector

What's your best-selling type of parquet; what's the average cost per square meter?

Most of our sales come from parquet in Oak (70%) Beech (15%) and Walnut (15%). Ukraine also

produces parquet in Acacia and Cherry. I think that Oak parquet represents the nation's finest quality. Retail prices per square meter range from 217 to 366 Hrivnie (38.92 Euro) for Oak, whereas Beech goes for 217 - 297 Hrivnie (34.31 Euro) and Walnut from 250 to 500 (50.06 Euro).

Is parquet common in Ukrainian homes?

Yes, it is. It's widely

used and considered the best choice, especially in the residential sector.

Is there a trade association for Ukrainian parquet producers and installers?

Yes, there is one, but we aren't members.

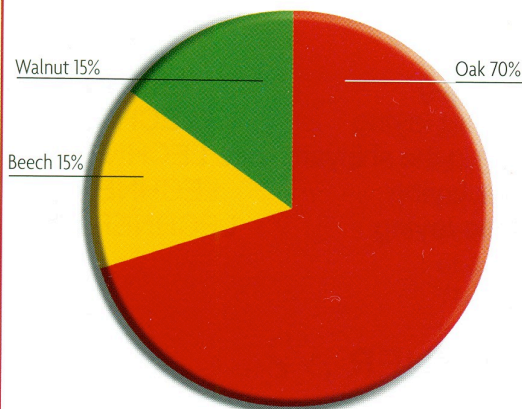
Do you sell much by Internet?

We've tried to make sales via Web in the past but without much success. Our clients like to touch the parquet products they buy first.

How are the banks? Do they help you grow?

Help from the banking sector is extremely limited here, and as far as I know, no specific products exist

**TYPES OF PARQUET SOLD IN UKRAINE**



Source: Report - Foreign Trade Ministry