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Evaluation of the position of Chernovtsy and Odessa regions of Ukraine with respect to economic performance and competitiveness and institutional capacity

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List of abbreviations

CBC	Cross Border Cooperation
CPI	Consumer Price Index
EBRD	European Bank for Reconstruction and Development
ENPI	European Neighbourhood and Partnership Instrument
FDI	Foreign Direct Investments
GDP	Gross Domestic Product
GoU	Government of Ukraine
GRP	Gross Regional Product
ILO	International Labour Organisation
IMF	International Monetary Fund
LFR	Local fiscal revenues
MoE	Ministry of Economy
MRDC	Ministry of Regional Development and Construction
NARDA	National Association of Regional Development Agencies
NNP	New Neighbourhood Programme
RCBI	Regional Capacity Building Initiative project
RDAs	Regional Development Agencies
RSAs	Regional State Administrations
SME	Small and Medium Enterprises
TC	Technical Cooperation
UAH	Ukrainian hryvnia
YoY	Year over Year

1. Introduction

This final report was prepared by EEO Group S.A., contracted by DG REGIO for the project N°2009.CE.16.0.AT.121, entitled "*Evaluation of the position of the Chernovtsy and Odessa regions of Ukraine with respect to economic performance and competitiveness and institutional capacity".*

This report gives an overview of the peer review process in the context of the aforementioned project. The report also provides further additional background information with respect to the three areas of assessment:

- Economic performance;
- Competitiveness;
- Institutional Capacity.

The report culminates in a set of targeted recommendations as to future actions.

2. Background

2.1. Overview of the Peer Review Process

The project commenced with a kick-off meeting held in Brussels on the 13th January 2010. The meeting outlined the framework of the assignment, the rationale and the possible challenges to the wider implementation of comprehensive regional development in support of the MoU. In the Month of January, 2010 a number of meetings were conducted in Ukraine to support the implementation of the peer review process. These included:

A. *Mr. Vacheslav Tolkavanov, Ministry of Regional Development and Construction (21 January 2010)*
   Was briefed on the assignment, its objectives and expected outcomes. He expressed support for the assignment, offered any assistance in the completion of the peer review, including any meetings and support that may be required.
B. *Mr. Dominik Pappenhiem, Sector Manager, Regional Development, EU Delegation in Ukraine (27 January 2010): Was briefed on the assignment, its objectives and expected outcomes.*
C. *Mr. Yuri Tretyak: Executive Director National Association of Regional Development Agencies (28 January 2010): Offered full support to the peer review team. Offered to assist in the elaboration of meetings in the target regions. Suggested that the mission should be held in April 2010, after the appointment of the new Oblast governors, the publishing of the regional contracts and sufficient clarity in the role of regional development in the post-presidential environment.*

During February 2010 significant resources were mobilised to prepare the peer assessment mission. Actions related to securing venues and ensuring the optimal participants attend the meetings required significant time and liaison with the Ministry of Regional Development and the National Association of Regional Development Agencies (NARDA) and the Regional Authorities in both target Oblasts. In both locations, a venue was tentatively booked (confirmed in March 2010) and a list of main actors invited.

In the month of February the Team Leader met again with Mr. Vacheslav Tolkavanov, Ministry of Regional Development and Construction (25 February 2010). At the meeting Mr. Tolkavanov was briefed on the progress of the assignment. He provided copies of a letter of support, signed by the Minister of Regional Development and Construction to support the actions of the peer review and pledged the support of his department to securing proper attendees and venues. It must be said that the Ministry has provided exceptional support and guidance during the preparation of the preparation of the mission.

In the month of March 2010, significant resources were applied to final preparations for the peer review mission which occurred from the 15th to the 20th March 2010. Due to the difficult, time consuming and unpredictable transportation connections (especially as this relates to Chernovtsy), travel by private bus was the most optimal mode of transport possible. The regional administrations of both Chernovtsy and Odessa were very helpful in the organisation of the events, with active participation from the public and private sector. Significantly, during the peer assessment mission, the governors of both oblasts were in the process of changing, a function of the Ukrainian political system which sees the President select governors. While this might be seen as a negative, participants were much more 'free' to express their views and interesting information was obtained by the peer review team.

Additionally, in the month of March (and in particular during the field mission) the main senior management of the Ministry of Regional Development and Construction either resigned or were replaced, including the Minister (Mr Kubida), Deputy Minister (Mr Tkratchuk) and Mr. Tolkavanov (the main point of contact for the MoU and this Peer Assessment mission). In addition, all staff related to the implementation of the MoU have been released from service, and replaced by new staff (mostly related to the construction function of the Ministry of Regional Development and Construction).

In preparation of the peer assessment mission a set of indicative questions were prepared and circulated to the participants. These were designed to assist the participants to prepare for active participation in the proceedings. A copy of the set of questions in included at Annex A of this document.

The **Peer Review** took place between **15th and 20th March 2010**. The programme of events was implemented as planned:

Monday (15th March 2010): The team has an initial briefing with the EC Delegation (Mr Dominik Papenheim and Ms Claudia Fischer). While meeting with the Ministry for Regional Development and Construction were anticipated, the change of senior management did not allow for this. The team travelled to Chernovtsy by mini-bus (10 hours). Mr Dominik Papenheim, travelled with the team.

Tuesday (16th March 2010): The team conducted the Peer assessment in Chernovtsy. The review was conducted in an all day session which focused on economic, competiveness and

institutional capacity issues. Due to travel requirements, all activities related to the peer review were completed during the same day.

The session was well represented with active participation of the attendees (who represented a broad representation of public, academic and NGO sector. Representation of the private sector was also significant by virtue of the nature of interconnectedness of business and public sector actors in Ukraine. In addition, the team met with the out-going governor.

A list of participants of the Peer Review in Chernovtsy is included at Annex B.

Wednesday (17th March 2010): Travel day (10 hours). Extensive discussions on regional development issues were held en route with respect to Chernovtsy which was important in assessment preparation for Odessa.

Thursday (18th March 2010): The Peer review for Odessa was conducted very successfully with in excess of 20 participants actively participating in both morning and afternoon sessions. Likewise, the session in Odessa was an active session, which provided invaluable information for the peer assessment team, both for what participants said and that which they didn't say.

A list of participants of the Peer Review in Odessa is included at Annex C.

Friday (19th March 2010), travel back to Kiev (5 hours). As Mr Dominik Papenheim travelled with the team and Ms. Fischer was not in Kiev on Friday 19th March, the requirement for debriefing the EC delegation was negated. Debriefing with the Ministry for Regional Development and Construction was not possible, as no senior staff were available to be debriefed.

Saturday (20th March 2010): A morning debriefing session was held with the team and the Team Leader of the Support to Sustainable Regional Development project (EC-AP 2006). Travel back to home country for Peer Review Experts.

A major aim of the two workshops / meetings were to conduct discussions with main stakeholders and conduct the peer review workshop to provide for exchange of experience and lessons with respect to the issues which are impacting economic development, the state of economic infrastructure and the status of the process of recent local government reorganization. To meet this aim, the workshops addressed several key elements/themes in different sessions. These included:

- **Regional Development Structures and Mechanisms** - Impact on Regional Development (Constraints and Opportunities);
- **Economic Development and Competitiveness** (Constraints and Opportunities) and its effect on wider regional development;
- **Priorities for regional development in Odessa/Chernovtsy region**s;
- Other Issues and Open Discussion – Including a discussion on the Danube Strategy.

Each session involved:

- Working through a set of key questions (elaborated by a lead expert), with facilitated debate (according to system selected by the focus region);
- Sharing experiences between peers;
- Conclusions, discussion of lessons learned, priority generic highlights for report.

2.1.1. Overview of the Chernovtsy Session

The location of the Chernovtsy oblast in the South-Western part of Ukraine is less than optimal. The smallest in Ukraine in terms of area (besides the two city-regions), one of the smallest by virtue of population and one of the poorest in Ukraine (GRP) and one of the most unfavourable from a trade perspective. The population of the region is approximately one million, out of which 12.5 per cent ethnically Romanian, 7.3 per cent, Moldovan and 4 per cent Russian minorities. Outmigration is significant, especially among young processionals, primarily driven by high unemployment among younger generation, mostly to other countries and less frequently to other places in Ukraine. The region provides only 0.5 per cent of country's industrial output and 1.9 per cent of agricultural production, although one third of the labour force is engaged in agriculture. Estimated productivity per person employed in agriculture equals on average one fifth to productivity in other sectors, and thus the low GDP per inhabitant in the region (in 2007 the lowest in Ukraine, equalling less than half of the country's average and slightly higher than one seventh of the GDP per inhabitant in Kiev) has its structural underpinnings.

While it would be expected that the region would be well positioned for trade with the EU through Romania, this unfortunately is not the case. While it is true that the region borders Romania – a member of the EU, the existing border regime is subordinated to strict Schengen rules, which severely hampers cross-border traffic. For example, only one of previously operational six border crossing remained after on-going preparations to join the Schengen zone in 2011. The region also borders Moldova – one of the least developed countries of Europe.

All this said Chernovtsy has potential for growth, although the barriers to growth are huge. The following assets define the region:

a. the **location of the region** and primarily the fact that it borders or is in close proximity to countries of the European Union, which is of major economic importance to the Ukraine;
b. the **economic sectors** of the region with some interesting "commodity" products that could add value to the regional GDP;
c. **natural resources** that could become the means for tourist and agro-tourist development.

The **location of Chernovtsy** creates important potential as a major transportation corridor in Western Ukraine, a fact that was repeatedly mentioned by participants in the peer assessment mission. Looking at the map of the Ukraine, it does appear that the region is on an important central axis, which should place it in an ideal situation. It provides a direct line to the Black Sea from the west of Ukraine (and the European market beyond). The

north south axis provides an important land transport connection between the markets of South Europe and Northern Europe. In addition, the region is in close proximity to two major neighbours of the Ukraine, Romania and Moldova, which have their northern border crossings at the Region of Chernovtsy. That being said, the regions transport network is in very bad condition and without a significant investment in the main transport networks (to rebuild and not only to repair) the route cannot be a viable transport route. The region is also separated from Western Europe (through Slovakia and Hungary) by Zakarpatska Oblast, and no major existing or planned international transportation corridors pass through Chernovtsy oblast from the West of Ukraine to the East. Moreover, the peripheral nature of the region is being exasperated by the on-going situation in Transdnistria, since the relatively important route (rail and road) connecting Chernovtsy with Odessa passes through Tiraspol (Transdnistria).

While the region has potential for "**commodity" production**, these are either not adequately exploited or completely wasted. With respect to agricultural production, most is exported in its raw or un-processed form. Agro-processing is not a major (in relation to its potential) aspect of production. Other economic opportunities exist, including: oil and gas reserves, wood resources and the acclaimed garden and vegetable products, as well as meat, milk and dairy production. Presence of foreign capital is limited. It was mentioned that only one large industrial entity was active in the region – producing machinery for oil and gas industry, and exporting mostly to Arab countries. While many other examples of commercial entities were provided by participants, most were from Kiev and utilizing concessions provided from Kiev. Participants added that the normal profile of investors reaching the region from other places of Ukraine usually have a short-sighted attitude – fast profits and relocation.

In general the development of Ukrainian regions is highly dependent on the national level, than on the regional tier. The oblast authorities do not have sufficient funds to finance regional projects related to economic development or infrastructure construction. The funds are – according to the statement of the outgoing governor – normally directed to road maintenance and to selected social projects, such as building schools, creating secondary homes for orphans and the like. It has been indicated that Chernovtsy oblast strongly depends on subsidies from the national government. Estimates indicate that the GDP created in the region would cover only two thirds of its expenses. However, this does not prevent the regional actors to claim more fiscal independence from the centre (e.g. "*we can very easily develop ourselves*").

The opposition of participants of the centre is clearly visible ("*everything that was done here – was done in spite of Kiev*"). It was claimed, and agreed by most participants, that the central authorities are an impediment to regional development and that the main central authorities responsible for regional development are more interested in fighting each other than implementing effective programmes. A strong appreciation of the lack of a clear division of competence between the Ministry for Economy and the Ministry for Construction and Regional Development (for example - the MRCD may approve a project, but the ME will not finance it) is strongly perceived as detrimental to decision-making in the field of regional policy. Also, it was mentioned that excessive centralisation –

especially in the field of cross-border cooperation - limits the development of regional development. As a result, it is indicated that there is no regional policy in Ukraine, and no regional funds for the regions. A majority of financial resources coming from the centre is earmarked for infrastructure (social and material), and not for business/economic development.

The region has a complex regional development strategy that was prepared by academics which collaborate with the oblast administration, which would not resemble a European or International document. For this reason, the region does not effectively possess any strategic document at the regional level. At the national level, the *National Strategy for Regional Development until 2015* is the main strategic document for regional development which links the wider legislative package supporting and regulating regional policy issues, including a law on "Stimulation of Regional Development". Unfortunately, the document is fundamentally a National Development Strategy and lacks the necessary regional framework and definition of regional development structures. In addition, institutional changes were described in terms of principles rather than concrete mechanisms for implementation. In addition, there is a striking lack of a national level legal framework on regional development.

The development of a comprehensive strategy for RD at both the national and regional levels is important in the next stage of the evolutionary process – in defining the next conceptual framework involving legal, institutional, administrative, and organisational development components required to facilitate regional development. While the national strategy is a complex process and outside the scope of this assessment, recommending the creation of a set of strategic document at the regional level, is possible. This step will take time and effort, including sustained efforts and commitment on behalf of the main international donors, and in particular the EC at a regional level.

With respect to cross-border cooperation, which is one of the few consistent and present opportunities for financial assistance ("*CBC money can solve the painful problem, a stimulus for further development*"), strong hopes are pinned on this source of regional funding. The participants indicated that the Romanian side, where the Joint Managing Authority (JMA) is located, is not seen as a fair authority, and in general is seen as concentrating most CBC funds in Romania (or in Moldova) and even not properly distributing information. Additionally, dramatic decrease of the number of border crossings (from six to one) has limited the opportunities stemming from the cross-border cooperation. All this puts in doubt hopes for using the CBC structures for development of international tourism, which may be a bit premature or unjustified due to peripherality of the region, its poor accessibility, underdevelopment of tourist infrastructure and low tourist competitiveness, even in comparison to other Ukrainian and Romanian regions.

The regional economic potential of Chernovtsy oblast is in general quite low. This is due to its following characteristics:

- **unfavourable location** and poor accessibility;
- **lack of modern economic sectors** and strong reliance on relatively backward agriculture and forestry;

- **unfavourable institutional settings for regional development** – strong centralisation, unclear regional policy, dependence on subsidies that are mostly directed to social sphere;
- **low opportunities of cross-border cooperation** – the region neighbours poorly developed regions of Romania and Moldova, with strong border regime of the EU;
- **underdeveloped local institutions** and lack of cooperation between regional administration and the NGOs;

This does not mean that opportunities do not exist, as was mentioned in the beginning of this section. It mostly relates to the fact that targeted and efficient allocation of resources is required which take advantage of the strengths and minimize the weaknesses. For that reason, a comprehensive analysis of the region and options (especially in the area of economic development, but also in the development of useful structures to sustain economic development) are critical. Assistance in the implementation of these options would also be required. Focusing in the short to medium term on economic opportunities related to agriculture and forestry, and examination of other options (building on existing strengths) would be critical.

2.1.2. Overview of the Odessa Session

The development process in the Oblast of Odessa is a paradox. The region should be one of the wealthiest in Ukraine for the following reasons:

- There is a **large and active harbour** that carries the majority of import / export activity in the Ukraine and even further (Byelorussia and Russia);
- It is the **most "European" region** of the Ukraine in terms of history, inhabitants, landscape, ancient sites, etc.;
- It is one of the most active regions with respect to **tourist activities** in Ukraine and a significant number of summer vacations take place in this region. Agro-tourism and alternative forms of tourist development have been developed and have potential for the region;
- There is a good basis of **entrepreneurial and SME activity**;
- **Natural and human resources** are in abundance in the region;
- **Cross border cooperation** and the proximity to Romania, Moldova and Turkey is an advantage for the region;
- It is one region with a competitive advantage in the **technology and biotechnology** sectors in Ukraine;
- The immense city of Istanbul (20 mil inhabitants) is only 1 hour flight away from Odessa and only half a day away by boat. Ferry and shipping Connections to Georgia (Asia), Bulgaria, Romania, Russia, etc;
- **Fertile land** (Black Earth) and a tradition of diversified agriculture is a positive asset for the region. Favourable climate and temperature make a wide range of agricultural production possible;
- Very good **transport connections** to Kiev and a wide range of international destinations (Istanbul, Vienna, Frankfurt, etc.)

Unfortunately these factors do not benefit the regional economy for the following reasons:

- All harbour activity is controlled and financial benefits accrue to the central government or organisations that are subordinated to the central administrations;
- A strong and effective development coordinating organization (such as an effective RDA in a European context) does not exist;
- The CBC structures are fractioned, weak and ineffective;
- Agricultural land is not efficiently cultivated and is underutilised;
- Tourist infrastructure is not well developed and a Tourism Master Plan does not exist;
- There is a limited promotion of the region to foreign markets and other countries both as a tourist destination as well as a strong development region in the Ukraine for foreign investors;
- Support structures for SME and entrepreneurship development are weak;
- There is lack in basic infrastructure for contemporary tools of support to entrepreneurship such as business incubators, innovation centres, business centres, technology parks, logistics services, etc.
- There is no clear objective in the development destiny of the region and no clear strategy to pursue such an objective.

It was possible to extract from the session and meeting with regional officials, that there is a lack of any significant regional structure that could lead development, investment, economy stimulation, attract and support FDI and of course coordinate all activities of cross border cooperation and development actions. There are numerous NGOs and structures (a few calling themselves Regional Development Agencies) which implement a number of small projects and overlook several activities, although they do not appear to belong to any comprehensive and integrated planning scheme directed towards the overall development of the region with a specific mandate. The team had a chance to meet a number of such agencies.

In the assessment meeting interlocutors from the development department of the Region of Odessa, the Development Agency of the City of Odessa, the Odessa Oblast Regional Agency for Reconstruction and Development, the Centre for Regional Studies, at least a couple of structures calling themselves Regional Development Agency and a number of small agencies and organizations in the sphere of activities of CBC were present. It is evident that all these agencies cannot become a powerful and dynamic element of development in the Odessa Oblast if they do not join efforts, combine their capacity, develop a common strategy and work together for the implementation of EU funded and internationally funded development programmes. At the same time, they will have to develop integrated and effective CBC programmes. Lastly, it is necessary to examine the policies and implementation of activities to support entrepreneurship and SMEs of the region.

It was mentioned in the meeting that over time there have been created “many good structures” of specialized agencies. These specialized agencies were short lived, existing as long as funding from external sources continued and rapidly dissolved afterwards. They

disappeared due to the lack of further funding and a deficit of funds from governmental structures or from private sources. Understanding the number of structures existing, the degree of competition and the crowding out effect, ensuring any funding for the continuation of a RDA structure would be difficult. Evidently, the experience gained, the capacity built and the human resources used for the implementation of the project lost any significance to further contribute to the development and growth of the region.

The establishment of an integrated RDA could be a good solution for the planning and implementation of a comprehensive ROP funded partially by the EU, the central state and the local authorities. As in many other countries, the RDA could be created with the participation of regional structures as members in the initial capital formation of the organization. Therefore, all the agencies and authorities will be represented and could contribute to the General Assembly of the organization. The management should be selected by the General Assembly but has to be independent so as to carry out the implementation of the policies. The input of capital from the partners could be a good source of funding for the capacity building of the organization while the influx of EU and Central Government funds for the management and implementation of regional policy projects could add management fees that could contribute to the strengthening of the agency, capacity building and human resources development. An RDA would be a major agency to lead rural development projects as well, including LEADER or LEADER+ type projects.

The participants expressed very modest priorities for the opportunities of economic development for the region in our inquiry on how the local experts and authority representatives see the future of the region of Odessa. Their assessment was that the present and future strategic strengths of the region are (a) **agriculture**, (b**) tourism** and (c) **transportation.**

It is evident that these are very general priorities given without much consideration of strategic development objectives and possibilities for exploitation. **Agriculture** is mentioned as important for the region because there is an abundance of good and fertile land. Yet, there was no significant explanation of how the farming that is being carried out mainly by small farming enterprises or individual farmers could develop into a major activity adding value to the region. Furthermore, there is no mention of the creation, promotion and development of agro-tourism activities, organic farming, etc.

Similar assessments apply to the **tourism** sector. The regional assessment is based on the good location of the Region of Odessa, the historic and architectural treasures of the region, the relatively mild climate, the high quality cultural activities and the existing tourist infrastructure. It is considered that these will suffice for tourism to become an agent of development for the region. In the mean time the tourist infrastructure is lagging behind in standards for receiving a sizable number of wealthier tourists, there is no promotion of the region in any of the tourist markets in Europe, there is no regional tourist identity nor tourism development strategy and lastly there is no organization or structure to coordinate and implement activities of promotion and support to tourism.

When it comes to **transportation** becoming a major asset for the region, once again the assumption is based on the fact that Odessa has a large and important harbour in the wider Black Sea region. This is true but the harbour's activity and income belong to the Central Government leaving very few opportunities to the region. Yet, even as such, the harbour could become a major income generating infrastructure with the development of parallel and complementary activities such as logistics, catering, servicing, etc. Once again, the appropriate structures that could support such efforts do not exist.

According to the testimonies we have had in the peer review it seems that the Region of Odessa might excel in the area of **Technology, Research, Biotechnology and CBC**. It seems that there is a good basis for higher education institutions and training centres with an abundance of highly skilled human resources. The marine technology and marine studies if further developed – apparently they are strong fields of research – could make Odessa a strong centre of research and education in the Black Sea area. At the crossroads from the Caucasus and Central Asian republics to the eastern and western European markets, Odessa could develop into a first class logistics centre as well as an energy transportation centre.

Apparently, one of the fields that could be important for Odessa region is that of the creation and development of logistics and services. Located very centrally in the Black Sea and in the south coast of the Ukraine, being a strong and important hub for the transportation of goods and people, the area could develop logistics centres, business parks, technology parks, innovation centres, educational and research facilities and of course marine technology and research centres.

The importance of the location in the Black Sea and in the south part of the former Soviet bloc could convert Odessa to the epicentre of activity. The congress and exhibition centre needs to be synchronized with the appropriate development of the much needed infrastructure. In combination with the beautiful city environment, the rich cultural heritage, the world renowned opera and the well developed entertainment and leisure facilities with an interesting and well developed consumer goods market, Odessa could attract the organization of congresses, exhibitions and organization of events. Such activities support the tourism industry and also add heavily to the value of local GDP.

3. Current Situation – Economic Performance, Competitiveness and Institutional Capacity

The timing of the mission was not optimal due to the Presidential elections and the widespread reorganization of the Ukrainian government which is currently underway. As a result of elections held on 7 February 2010, now President Yanukovych (48.95%) defeated Prime Minister Yulia Tymoshenko by a margin of approximately 3.5%. President Yanukovych was sworn in on 25th February 2010 and became the fourth president of Ukraine. Consequently, a re-organisation of the parliament has resulted in the Party of Regions securing a majority, and the post of Prime Minister. This establishes clear political stability, although the direction which this new stable government will take in the context of regional development and its relationship with Europe, is not yet clear.

Regaining political stability is particularly needed in Ukraine, whose economy was hit severely by the international liquidity crisis. In 2009, real GDP fell by 15% yoy, one of the deepest declines in the world. Although the economy started to show signs of improvement in the second quarter 2009, the recovery was rather slow. The beginning of 2010 was encouraging as Ukraine's industrial sector reported almost 12% yoy growth on the back of rebounding external demand for Ukraine's exports. On the other hand, domestic demand is likely to remain subdued, exerting a toll on economic growth, forecast at a moderate 3% yoy in 2010.

The following section describes the current situation with regard to the general economic framework in Ukraine and regional development in the two selected regions of Ukraine.

3.1. Current Economic Framework – National Level

Being a very open economy, with exports accounting for approximately 50% of GDP (with a high reliance on commodities), Ukraine is exceptionally affected by changes in external demand. While the global economic slowdown of 2008-2009 had a strongly negative effect, a rebound of demand has a conversely strong positive effect. Therefore, Ukraine is forecast to benefit from the expected stronger rebound of external demand in 2010. Industrial production grew by 11.8% yoy in January 2010, driven by export-oriented metallurgy (+26.6% yoy), chemicals (+29.5% yoy) and machinery (+22.3% yoy). The industries benefited from a mix of reviving external demand, improved competitiveness due to sharp Hryvnia depreciation in the fall of 2008 and government stimuli (gas price subsidies to chemical enterprises, preferential cargo transportation tariffs for metallurgical and mining companies, etc.). Favoured by a strong rebound in metallurgy, production of iron-ores and coking coal went up by 33.7% yoy and 17.4% yoy respectively. The revival of Ukraine's foreign trade and manufacturing underpinned an almost 16% yoy increase in cargo transportation. Agriculture, which was virtually the only sector demonstrating small but positive growth in 2009, continued to show positive activity at the beginning of 2010.

While exports are expected to be the main driver of economic growth in 2010, its strength may not be sufficient to compensate for domestic demand weaknesses. In addition, Ukraine's exports may be hampered by intensified competition on foreign markets amid relatively high dependence on imported raw and energy materials and narrow product and geographic diversification. Furthermore, to a notable extent January's upsurge was attributed to an extremely low statistical base. Indeed, January 2009 was the toughest month in terms of output decline in most sectors. Thus, industrial production fell by 33.8% yoy, with metallurgy, chemicals and machine-building demonstrating the sharpest rates of decline (-45.7% yoy, -49.8% yoy, -56.8% yoy respectively). Although the impact of the low statistical base effect will be felt throughout all of 2010, it will notably ease through the end of the year. At the same time, the stronger rebound of the world economy, quick stabilization of the political situation and reasonable progress in reforms are among the upside risks to the forecast.

For 2010 and 2011 both the WB and the IMF forecast a continuation of the economic recovery in Ukraine. The WB and the IMF forecast much more moderate real GDP growth than Ukrainian economic assessments due primarily to different assumptions on the activity on international capital markets, related to higher risk aversion assumptions on international capital market and as a result less active investment activity, than Ukrainian economic institutions. All forecasts predict that real GDP in 2011 will not reach 2008 levels (with decline by 4.9% according to the WB forecast, 4.2% according to our estimate and 2.8% according to the IMF forecast), although solid recovery is anticipated.

3.1.1. Major parameters of the forecasts[1][2]

	World Bank			IMF		
	2009	***2010***	***2011***	***2009***	***2010***	***2011***
Nominal GDP, UAH bn	991	1104	1253	990	1118	1240
Real GDP, %	- 9.0	1.0	3.5	- 8.0	1.0	4.3
Real domestic demand, %	-	-	-	-18.8	2.2	5.6
Real consumption, %	-18.8	2.3	4.5	-	-	-
Real fixed investments, %	- 31.4	2.6	10.6	-	-	-
Real export, %	- 10.1	1.1	2.1	-	-	-
Real import, %	- 34.3	2.4	7.6	-	-	-
Real goods export, %	-	-	-	- 8.8	5.8	-
Real goods import, %	-	-	-	- 31.8	5.6	-
GDP deflator, %	14.6	10.3	9.7	- 30.9	7.8	6.1
CPI, %[3]	16.4	10.0	7.9	16.0	8.0	6.0
CPI, % [4]	-	-	-	17.2	10.8	7.0
Current account balance, USD bn	-	-	-	0.6	1.5	-1.2
Current account balance, % of GDP	0.3	0.5	-0.6	0.5	1.2	-0.9
Goods exports, %	-	-	-	- 28.8	8.3	9.1
Goods imports, %	-	-	-	- 39.2	5.1	12.3
Goods terms of trade, %	-	-	-	- 13.6	3.0	-2.0
Services terms of trade, %	-	-	-	- 9.2	5.7	-0.6
Terms of trade, %	-7.7	1.2	-0.2	-	-	-
FDI, %	-	-	-	4.6	4.6	5.3
Budget revenues, % of GDP*	41.5	41.9	42.0	41.4	43.0	43.0

[1] Source: Ukraine Economic Update, April 7, 2009, the World Bank; The IMF, Ukraine: First Review Under the Stand-By Arrangement, Requests for Waivers of Nonobservance of Performance Criteria, and Re-phasing of Purchases Under the Arrangement - Staff Report; Staff Supplement; Press Release on the Executive Board Discussion, May 2009; IER estimates

[2] All figures year on year unless otherwise stipulate

[3] End of period (eop)

[4] Average over period (aop)

	World Bank			IMF		
	2009	*2010*	*2011*	*2009*	*2010*	*2011*
Budget expenditures, % of GDP*	44.5	44.2	44.3	44.3	43.5	43.5
Fiscal balance (w/o bank recap), % of GDP	3.0	2.3	2.3	4.0	1.9	1.9
External debt, % of GDP	89.3	80.7	69.3	87.0	82.6	75.9
Public and Guaranteed Debt, % of GDP	28.8	29.2	30.0	32.5	31.1	29.0

3.2. Regional (Oblast) Level Economic Assessments - 2010 through 2011

3.2.1. Gross regional product (GRP): A Regional Outlook

Ukraine, being a large geographically diverse country, is composed on a variety of economic activities which perform differently in terms of economic dynamism (real growth) and statistically (gross regional product per capita), especially in the face of economic challenges. The per capita income of the wealthiest Ukraine's region - Donetsk[5] - (UAH 12 490), which 33% higher than Ukraine's average – UAH 9 372 while the poorest region, Chernovtsy, earns less than half of the national average[6] - UAH 6 474. There is no significant correlation between wealth and rate of growth of a region, as the wealthiest region (Donetsk) grew at a rate of 4.6% in 2007 (less than average) and even experienced a decline in 2005 of (minus) – 2.9%. Conversely, the poorest region, Chernovtsy, demonstrated one of the highest growth rates (8.3%) in 2007. In 2007, Volyn oblast was the most rapidly growing region (12.1%), while Kirovohrad oblast experienced a decline (2.1%). At the same time it is difficult to trace any trend in the regional growth although there is a strong relation to the main economic activity, as there tends to be a low level of economic diversification in Ukraine, especially in its regions.

Gross Regional Product (GRP)*:* Economic development in Ukraine is not consistent in all regions. The factors determining the level of regional economic development are primarily the sectors of regional specialization, which in the broad context of Ukraine can be diverse. With respect to regional value added, the most important sectors are: manufacturing, trade, transport, real estate, and agriculture. During recent years, the share of agriculture in regional value added has declined in all regions due to increases in manufacturing, trade, and real estate. In 2006, eight regions specialised in agriculture, fourteen focused in industrial production, four in trade and one in transport. At the same time, the number of regions specializing in agriculture dropped in 2007 against the background of a decline in real value added in this sector. In 2011, it is expected that eight regions will specialise in agriculture, sixteen regions in manufacturing, and as previous, and four regions in trade and one in transport.

Ukraine can be differentiated as primarily industrial and mostly agricultural regions of Ukraine. For instance, 72% of industrial output is concentrated in twelve regions, mostly in

[5] Income of the city of Kyiv is higher – UAH 28 780.

[6] The Ukraine competitiveness report 2008, World Economic Forum.

the east of the country, 38% of which - in Donetsk and Dnipropetrovsk regions[7]. On the other hand, most agricultural output is concentrated in the five geographical central regions. As different regions have different regional economies, changes in the macroeconomic environment create different responses. For instance, regions that specialized on export oriented activities (e.g. metallurgy, machine building and chemicals production) depend heavily on prices and conditions on the international markets. On the other hand, economic performance in agricultural regions depends primarily on the weather fluctuations and more on government policy with respect to international trade.

Table A: Gross Regional Product: A Regional Outlook

	Real Gross Regional Product (% YOY)					GRP per capita (UAH)				
	2007	**2008**	**2009**	**2010(E)**	**2011(E)**	**2007**	**2008**	**2009**	**2010(E)**	**2011(E)**
Ukraine	**107.9**	**102.1**	**87.1**	**104.0**	**107.3**	**15496**	**20614**	**20487**	**25383**	**30597**
Chernovtsy	108.3	102.7	91.2	103.3	105.4	7369	9868	10148	12516	15077
Odessa	106.3	110.1	90.0	103.9	106.2	13827	19436	19392	23597	27878

Source: Institute for Economic Research (IER), Macroeconomic and Regional Development report of Ukraine, Jan 2010

3.2.2. Unemployment and wages: regional outlook

According to the ILO definition, the level of economic development of regions defines the unemployment rate and the level of wages. In 2007 and 2008, the highest unemployment rates in Ukraine were in Rivne oblast, which was followed by Ternopil, Chernovtsy, and Zhytomyr oblasts. Overall, in sixteen out of Ukraine's twenty seven regions, the unemployment rate was higher than Ukrainian average. The lowest unemployment rate was in the cities of Kiev and Sevastopol, as well as in the AR Crimea, Odessa, Dnipropetrovsk and Kharkiv oblasts.

Nationally, the unemployment rate has been declining for the last years, but increased in the fourth quarter of 2008 against the background of the current economic slowdown. Unemployment rate changes were similar in all regions, declining both in developed and 'depressed' regions, with the annual unemployment rate forecasted to be 9.5% for 2009. The unemployment rate increased sharply in such industrial regions as Donetsk, Kharkiv, Dnipropetrovsk oblasts, while in some agricultural regions (e.g. Mykolayiv and Kherson) unemployment increased at a slower pace, as agricultural sector is expected to suffer less from the crisis. The sharpest increase in unemployment is expected in regions with high share of metallurgy, machine building, manufacturing of other non-metal products and chemical production. In particular, unemployment rates in Donets and Vinnitsa oblasts are expected to be higher, while Luhansk and Lviv are expected to have lower levels of unemployment.

Economic recovery is expected in 2010, which should result in reduction of the average unemployment rate, which are forecasted at 8.6% in 2010 and 7.4% in 2011. The unemployment rate will decline in all regions with higher rate of contraction in

[7] Social and Economic Development of Regions of Ukraine: January – December 2008, Ministry of Economy http://www.me.gov.ua/file/link/129084/file/01-12_2008AP.rar

economically developed industrial regions, reflecting the expected recovery in metallurgy, machine building and other industries.

***Wage developments*:** Between 2000 and 2008, the average wage in Ukraine increased in excess 3.5 times in real terms. Wages increased rapidly in all regions with higher growth rates in less developed regions. As a result, during the last years there was a trend to wage convergence, though high wage disparity remained. The employees in Kiev city traditionally receive the largest wage. Among regions, in 2007 and 2008 the highest wages were paid in Donetsk, Dnipropetrovsk, Zaporizhzhsa and Kiev oblasts. The wages in the rest of oblasts were lower than Ukrainian average. Lowest wages were paid in Ternopil, Volyn, Chernovtsy and Kherson oblasts.

Table B. Unemployment and wages: regional outlook

	Unemployment [8]					**Average wage** UAH				
	2007	**2008**	**2009**	**2010**	**2011**	**2007**	**2008**	**2009**	**2010**	**2011**
Ukraine	**6.4**	**6.4**	**9.5**	**8.5**	**7.5**	**1353**	**1809**	**1896**	**2100**	**2400**
Chernovtsy	8.6	8.4	10.4	10.3	8.9	1052	1409	1488	1634	1868
Odessa	4.4	4.5	7.4	6.3	5.7	1227	1636	1749	1939	2215

Source: Institute for Economic Research (IER), Macroeconomic and Regional Development report of Ukraine, Jan 2010

3.3. Fiscal indicators

Fiscal revenues at the regional and local level in Ukraine consist of own and ceded taxes and duties, non-tax revenues, capital gains as well as transfers of various kinds. According to the Budget Code of Ukraine, revenue sources are assigned to local government entities (LGEs) for the fulfilment of their own and delegated responsibilities. At the same time, own revenue sources are destined to cover expenditures on own responsibilities only. Revenues and expenditures on delegated responsibilities are estimated by the Ministry of Finance. Nevertheless, LGEs are able to collect and spend larger (bigger) amounts. The purpose of MoF's calculations is to define the amounts of transfers to cover the gap between estimated revenues assigned to delegated responsibilities and estimated expenditures on delegated responsibilities.

A high dependence on central government grants and low fiscal discretion are typical for Ukraine, as for many other transition economies. After 2002, when inter-budgetary fiscal relations have been arranged in accordance with Budget code, 88% of oblast budgets proved to be transfers dependent. In 2005-2007 the share of transfers was 36-40% of the total regional revenues. Traditionally, Donetsk and Dnepropetrovsk regions as well as Kiev and Autonomous Republic of Crimea are net contributors to national revenue while other industrial regions, including Zaporizhzhsa, Kharkiv, Odessa, Poltava oblasts are normally net contributors. The remaining oblasts are net recipients.

Local fiscal revenues (LFR) in 2009 are forecast to decrease by 12%[9] to UAH 121.0 bn in nominal terms. In relation to consolidated budget revenues they are anticipated to decline

[8] **ILO methodology -** % of population between 15 and 70 years old

from 46% in 2008 to 44% in 2009. Simultaneously, LFR share in GDP are expected to drop by 1.4% to 13.0%[10]. In particular, Personal Income Tax (PIT) revenues are expected to drop due to increase of tax deduction against the background of equalization of the minimum wage to the subsistence minimum set for working able individuals[11].

Gradual recovery with respect to local revenues and expenditures in 2010 -2011 is expected with local revenues projected to grow by 17.65% and 25.6%, respectively with their share of the consolidated budget revenues increasing by 47.0% and 48.7%. This is expected as a consequence of the anticipated adoption of new edition (version) of Budget Code, which is expected to come into force in 2010[12]. The new budget code envisages promotion of local financial autonomy and the improvement of the formula for the calculation of financial transfers. Based on these revisions, local budgets will have additional receipts including 15% of the enterprise profit tax, 50% of the tax revenues over-execution amount and receipts from some licensing duties, which were previously assigned to the State budget. It will broaden to some extend the revenue base of regional budgets in 2009-2010. Besides, as agricultural sector is the least damaged by the crisis we expect higher revenue growth for the agricultural regions compared to industrial regions. These regions, primarily, Poltava, Vinnytsa, Kirovograd Kherson and Kharkiv oblasts will have surplus of their budgets in 2010-2011. Positive cash balance are also envisaged for regions with high potential for tourism development and oriented to the implementation of infrastructure projects. Kiev budget will have deficit in 2010-2011 as the local authorities will have more chances to borrow money in external and internal markets to cover their capital expenditures.

3.4. Institutional Capacity Assessment – National Regional Development Structures

One of the main challenges with respect to the current state policy to support regional development is the number of structures responsible for regional development and the lack of a clear institutional system for decision-making and the lack of united coordination and managerial division of responsibility. While these two main structures (MRDC and MoE) have primary responsibility for RD, a group of central administrative structures of the GoU or national advisory and consultative structures that influence state policy on local self-government and regional development. These include:

Ministry of Regional Development and Construction (MRDC) is, with the Ministry of Economy, directly responsible for regional development planning and implementation. In general, the MRDC's mission and role as the lead government body in Regional Development are defined by the Regulations on MRDC approved by Resolution of the Cabinet of Ministries of Ukraine "Questions related to the Ministry of Regional Development and Construction"[13]. These Regulations do not provide a short definition of

[9] yoy

[10] However, for each regional budget the corresponding shares will grow by 2.0% in average.

[11] IER, Macroeconomic Forecast of Ukraine, No.5 (21), May 25, 2009

[12] On 24th of June 2009 the Verkhovna Rada of Ukraine adopted a Law "On Introducing Amendments into the Budget Code of Ukraine'.

[13] Resolution No 750 dated 16 May 2007

purpose, operational role and values of the ministry which is usually referred to as 'mission of the organization'. Instead, it includes a quite detailed description of the tasks, functions and activities performed by MRDC. Based on this information it is possible to extract the purpose and operational role of the organization from this description. The Regulations on MRDC establishes that MRDC's regulatory tasks in the regional development include the developing and the making of proposals related to deconcentration and decentralisation of authority of central and local bodies of power as well as participating in development and implementation of the legal, economic and organisation mechanism of adjustment and stimulation of sustainable development of regions. MRDC also has authority to adopt secondary legislation such as regulations, instructions, norms, etc.

Ministry of Economy (MoE): The main tasks of the Ministry of Economy are to participate in the formulation of state regional policy and to coordinate its implementation. The Department for Regional Development is the main administrative unit in the MoE responsible for the implementation of regional policy. The main purpose of this department is to formulate proposals and to implement state policy on the creation of conditions for regional and local development, the intensification of potential of regional resource and the strengthening of regional compatibility.

Secretariat of the Cabinet of Ministers of Ukraine (primarily the Department on issues of Interaction with Local 'Power' Bodies): The main tasks of this department include: the management and analysis of the government activities in relation to the provision of organizational, methodical and other practical assistance to local bodies in the implementation of governmental policy in relevant areas; the monitoring and analysis of the organization of local executive power bodies in terms of the implementation of state regional and personnel policy; The organization of issues related to the Interdepartmental Commission on Local Self-government attached to the Cabinet of Ministers of Ukraine, the Commission on Administrative and Territorial Arrangement Issues and other advisory bodies in terms of their work on local executive power bodies and self-government bodies issues, which are established by the Cabinet of Ministers of Ukraine; and the coordination of actions related to improving the normative and legal basis for regulating the activities of local executive 'power' bodies and local self-government bodies.

National Council for State Construction, Local Self-government and Regional Development (Advisory and Consultative Body): The main tasks of the National Council are to formulate and make proposals on determining the priorities and mechanisms of state policy on state creation, local self-government and regional development, integrated implementation of administrative reforms, administrative and territorial reform, and local self-government reform; to develop civil society, forms of direct democracy, and an improved system of interaction between government bodies, local self-government bodies, their associations and other unions, public organizations, and business structures; to ensure the activities of administrative structures (power bodies) are transparent and citizens are involved in the formulation of nationally and locally significant decision-making; and to assess efficiency.

Secretariat of President of Ukraine: The Main Services of Administrative and Legal Policy and Regional and Personnel Policy are established within the structure of the Secretariat of the President of Ukraine, which was approved on March 24, 2005.

Foundation for Local Self-government of Ukraine: The Foundation for Local Self-government has been (since 1996) the central state scientific and methodical, advisory and coordinative institution on local self-government development. In particular, the Foundation has directly participated in the formulation of the draft of the Constitution of Ukraine (specifically the sections concerning the organization of territorial power in Ukraine), the draft of the Law of Ukraine "On Local Self-government in Ukraine", and the draft of the Concept of Administrative Reform.

National Association of Regional Development Agencies (NARDA) in Ukraine is the main non-governmental actor with the most significant resource in regional development. NARDA's mission is to efficiently coordinate state regional policy and its own regional development policy through the systematic realisation of its functions through NARDA's own efforts and resources and to coordinate actions of its members.

Regional Development Agencies: Regional Development Agencies (RDAs) emerged in Ukraine in the mid 1990s, with their relative position and effectiveness gradually improving since the adoption of the Constitution in 1996 and the Law on Local Self-Government in 1997. Today, RDAs exist in every Oblast centre, as well as in many smaller towns, with most RDAs established as autonomous, non-governmental organizations. The first RDA was created in the city of Zaporizhzhya in 1993, and most of the RDAs currently operating were created between 1996 and 1999. They vary widely in terms of organizational capacity. In most cases, RDAs were initiated by groups of people from small businesses and community organizations that saw a need to organize more effectively to promote community led sustainable development through the wider participation in local and regional policy development and implementation. In many cases, these RDAs have received support from local authorities and/or local businesses.

Regional State Administrations (RSA): RSAs are responsible for the implementation of state policy at the regional level (in accordance with the Law of Ukraine "On Local State Administrations"). In accordance with the Law of Ukraine "On Local Self-government", the district and regional councils are local self-government bodies representing the mutual interests of the territorial communities of villages, settlements and towns. However, according to the laws mentioned above, rayon and regional state administrations do not have tangible practical authority and resources to formulate and implement program documents and strategic solutions regarding the development of rayons and regions.

Participation of non-government bodies in the sector

There are different formats of participation of non-government bodies in regional development in Ukraine, which includes:

- Public Councils
- NGOs based on Law of Civil Associations
- Working groups established at various levels

Public councils may be created under each body of executive power at central and local levels. The institute of public councils was introduced in 2004 by the Cabinet of Ministries as part of the policy making process in government and a Cabinet Regulation[14] set up the requirement for public consultations in connection with the formulation and implementation of state policies.

The organization and tasks of the MRDC Public Council is defined by the Order of MRDC No20 dated 22 January 2009. The MRDC Public Council is a permanent consultative-advisory body, based on a regulation of the MRDC which was adopted by the same Order which states that council was created for the purpose of coordinating activities related to public consultation on policy implementation as well as including public opinion in the process of preparation and implementation of ministerial decisions. Chapter two (2) of the Regulations of the MRDC Public Council specifies the main tasks of the council in relation to regional policy:

- Participation in development and implementation of activities related to state regional policy;
- Secure the feedback from civil society organizations in relation to ministerial performance;
- Improvement of mechanism of collaboration between MRDC and civil society organizations, media and scientific institutions as for the implementation state regional policy.

Chapter three (3) of the same document specifies the rights and obligation of member of the MRDC Public Council. This chapter also includes the functions of the Council. Among the functions determine in the Regulations are:

- developing the draft plan of public consultations;
- conducting expertise of drafts of normative acts developed by the ministry;
- to advise on decisions made by the ministry;
- public scrutiny of the implementation of the ministerial decisions.

As of June 2009 there are 34 members of the MRDC Public Council who are divided into 2 committees:

- Committee on issues related to regional policy and local self-government - includes 8 representatives of non-government bodies, 2 mayors of small towns and 3 representative of government organizations;
- Committee on urban development, construction and architecture (the functions of which are not directly related to this study).

Another format of stakeholder participation is based on a general law on non-government organizations. The legislation of Ukraine – specifically, the Law on Civil Associations No. 2460, of 16.06.92 (amended) – provides a possibility for non-government organizations to be established and operate at central and local levels. Nevertheless, the current legislation does not envisage any specific and clear-cut procedure for such organisations to participate in the regional development area (sector). NGOs and/or civil associations may

[14] Cabinet Regulation No 1378 dated 15 October 2009

take part in all aspects of regional development either on their own initiative or by arrangement between themselves or with public administration bodies, or on invitation of the latter.

In practice, the participation of civil organisations in regional development, while allowed and possible, are currently reduced to only passive performance of certain requested consulting functions. It should be specifically noted that NGOs most proactive at the regional level (particularly those that have been established with primary focus on local regional developments) show more outreach capacity and really affect regional development. Some of these even have this reflected in their relevant titles – like Regional Development Agencies – and have an umbrella organisation, the Regional Development Agencies Association[15] established at the national level. Their activity depends more on the format of individual agreements than on legal activity framework.

Thus, the scope of authority of respective local state administrations that may relate to the regional development area also includes: development and performance of social and economic development programmes, target programmes, and regional development strategies. To provide for the above authority at the Oblast level, structural units of Oblast state administrations and administrative offices of Oblast state administrations must perform a whole range of managerial functions envisaged in respective statutes of these bodies of government.

The role of oblast council is determine by its decision making power. Under the laws in force, specifically, the Laws of Ukraine: on State Forecasting and Elaboration of Programs of Economic and Social Development of Ukraine (No 1602-III, of 23.03.2000); on State Target Programmes (No. 1621, of 18.03.2004); on Stimulation of Development of Regions (No. 2850, of 20.12.2005), regional development strategies, regional programmes, and the full list of national and regional programmes implemented with funds from Oblast budget must be approved by a respective regulation in the form of an Oblast council decision. The draft of such a decision is generally prepared by the initiating entity which is the structural unit of Oblast state administration.

3.5. Competitiveness (National Level and Regional level in both Odessa and Chernovtsy

According to the Foundation for Local Governance (FLG) annual report, Ukraine was ranked 72nd in the global competitiveness rating for 2008–2009 with a score of 4.09, between such developing countries as Morocco and the Philippines. As can be expected a significant gap exists between Ukraine and EU-12 countries (average score of 4.29 and 49th position in the ranking). At the same time, on a positive note the distance in the competitiveness ranking between Ukraine and new EU accession countries is shrinking (last year, the difference between Ukraine's overall ranking and the average EU-12 ranking was 0.36 points; in 2008–2009 it was reduced to 0.2 points). This shows that during the last year Ukraine managed to move closer to Central and Eastern European (CEE) countries in its competitiveness. If this rate of convergence continues, it could become one of the main arguments in favour

[15] http://www.narda.org.ua/

of granting the country a clearer EU membership perspective. In particular, among EU-12 countries Ukraine outperformed Bulgaria (ranked 76th) while lagging slightly behind Romania (ranked 68th).

The basic principle of regional competitiveness is that competitive regions cannot exist without competitive businesses, and competitive businesses cannot thrive in regions that fail to enhance private sector competitiveness. This is of fundamental importance. Unfortunately the environment in which businesses operate in Ukraine is increasingly arbitrary and difficult. With respect to the Doing Business 2010, based on OECD data, Ukraine place 142nd out of 183 countries. With respect to many of the other aspects of the survey, Ukraine places low with respect to middle income countries. A full statement of the data can be found at http://www.doingbusiness.org/exploreeconomies/?economyid=194. In general, the position of Ukraine from a competitiveness point of view is weak, being related to regulatory environment, the weak and arbitrary nature of the judicial system, weaknesses in the legal environment, and serious problems with taxation (including recent failures for the central government to repay VAT rebates). Being a highly centralised country, the challenges with respect to competitiveness at the national level very closely mirror the situation on the oblast level.

4. Recommendations

4.1. Individual Recommendations of Peer assessors (including Team Leader)

The project team is composed of two experts: a Team leader and a Junior Expert supplemented by a team of five (5) expert peer assessors. This team represented a highly experienced team with a wealth of practical and current experience in Ukraine and in Regional Development, as well as having existing solid working relationships with the ministries and regional structures of the GoU and its regions.

The experts Recommendations are outlined below:

1	**Colin Maddock, Project Team Leader**
	Recommendations: 1) An assessment of regional development requirements in regions, involving a comprehensive analysis of existing capacities (economic and institutional), barriers (and recommendations on how to overcome barriers) and recommendations on how to maximise economic opportunities. These should form the basis of future EC and other donor initiatives in the region. This is urgently needed and must be done in a comprehensive and effective manner; 2) Based on a comprehensive assessment, the development of a comprehensive and realistic strategic document (Regional Development Strategy) would be optimal and provide a strategic direction to the region(s); 3) Additional technical assistance in the implementation of the MoU between Ukraine and DG REGIO; 4) Increased technical assistance - support (concept development, project preparation, application development, financial management, effective execution) to assist regions to maximise impact of Cross Border Cooperation and other EC/other donor interventions; 5) Development of sound regional development structures which are well staffed, well resourced, and connected in a practical way to provide a network of regional development structures. Clear support in understanding these basic concepts (at both the national and regional level) is additionally critical.
2	**Dr Jon Bloomfield, Head of European Policy, Advantage West Midland, UK** **……Honorary Research Follows, College of Social Sciences, Birmingham University**
	Recommendations: 1) Regional development will be severely hampered unless urgent attention is given to road and rail infrastructure. 2) Much more rigorous regional economic strategies with a tighter focus on priorities have to be prepared. Recognise that existing strategies may have to change. 3) Concentrate economic efforts on areas of real potential 4) There is an urgent need to introduce a regional development function which should be based on sound partnership principles

5) Within Ukraine, the EU should focus its priorities more sharply. In particular, it should concentrate more of its resources onto regional development, as well as strengthening its cultural dimension.

3	**John Gallagher, Consultant, Regional Development Consultant, Ireland**

Recommendations:

1) Agriculture Development: The establishment of an integrated Oblast information, advisory and training service which will respond to the needs of farmers and support them in improving productivity The establishment of other supports to farmers (extension, farm support, co-operative development, etc.)
2) Tourism: The development and promotion of Tourism Brands, which would promote both Oblasts as quality tourism destinations (*Although it should be noted that Odessa given its range and mix of tourism products has more potential in this regard).* The development of a master plan for the development of costal tourism in Odessa is also important. The development of Odessa as a location for Business Tourism *(International Fairs & Conferences)*
3) Business and SME Development: The provision of an integrated Oblast business support service encompassing information, advice, guidance and training. Development of rural enterprises to counteract future increasing productivity in agriculture and resulting decreasing employment opportunities. *(The EU Leader Model could be considered as an approach).*
4) Academic and Research: The development of incubator spaces in the Universities of both Oblasts to facilitate and support the start up on new knowledge based enterprises. *(Although it is recognised that following comments by one Professor in Chernovtsy that standards are low and it also appears that very little academic research is being published internationally in both institutions that this could be a challenge.).* The targeting of existing Oblast SME support funds to support enterprises with growth and export potential. *(The Odessa Oblast highlighted they had a SME fund but it did not appear to be targeted on any sector in particular);*
5) A study should be undertaken to determine the potential for the establishment of a international financial services centre in Odessa. *(In addition consideration should be given to the establishment of a New Odessa Port Authority with Directors drawn from Odessa City, Odessa Oblast, Private Sector & Ministry of Transport representatives to ensure an integrated and co-ordinated approach to the future development of this strategic asset.)* Complete a review of the existing RD structures including:
    - An analysis of structures, competencies and functions as well as human
    - Resources and budgets of oblast departments engaged in economic development
    - A comparison of the situation with similar regional public administration structures in other countries *(benchmarking),* and determine the necessity for new institutions
    - Elaborate recommendations for increased efficiency in the economic development departments and for enhancing the ability of Oblast Administrations to actively contribute to the development of their Oblasts

4	**Alkis Papademetriou, International Programmes Director, Chamber of Commerce and Industry of Drama, Greece**

Recommendations:

1) An integrated RDA could be a good solution for the planning and implementation of a comprehensive ROP funded partially by the EU, the central state and the local authorities. As in many other countries, the RDA could be created with the participation of regional structures as members in the initial capital formation of the organization. In addition, support the creation of structures that could support entrepreneurship, private initiative and SMEs in the region.

2) A well organized and functioning "Euroregion" will be able to better negotiate the CBC programmes with Romania and Moldova, prepare good projects and have the capacity and means to manage and implement CBC projects. Using the Association of European Border Regions (AEBR), a pan-European association of support to cross border structures, could contribute to the effort of re-organizing the "Euroregion" in the Odessa Oblast to more effectively develop CBC and Danube Strategy.

3) More investigation is needed in order to draw safe conclusions regarding effective economic development but there are several sectors that could become important in terms of economic activity and also attract FDI.

In Chernovtsy, these sectors could be:

- energy resources that the locals claim the abundance of in the region
- the processing of milk to be sold in the large markets of Kiev and Odessa and the export of dairy products to EU countries to be marketed as natural and organic products from a pollution-free, clean and nature rich area in Europe
- garden products, vegetables and fruit produced in the area could be marketed as organically grown products in a protected, pristine, natural environment
- water resources could become an important regional income bearing activity
- wood could add value to the local GDP, especially if the wood is exported processed and not as lumber as it is today

In Odessa, in addition to the main sectors mentioned in the assessment (tourism, transport, agriculture), the following main areas may be interesting:

- creation and development of logistics and services centre.
- fishing and fish farming in the sea as well as in the rich in water ponds and rivers region

5	**Grzegorz Gorzelac, Director EUROREG, University of Warsaw, Poland**

Recommendations:

1) Delivering objective, modern knowledge on regional development and regional policies to the most important regional and local actors, as well as to the researchers active in this field.

2) Employing in the process of regional strategy building external experts who would be able to prepare an objective diagnosis of the region's potential and formulate proper strategic development goals and to overcome unrealistic attitudes and hopes.

3) Assisting the regional and local authorities in realistic assessment of development opportunities and potentials of their region and in modern territorial promotion.

	4) Improving functioning of euro-regional structures through better distribution of powers and responsibilities within the managing bodies, objective evaluation of past activities and utilising its result for planning future ones. 5) Demonstrating, on few concrete cases, possibilities for collective action of economic agents – e.g. in processing agricultural products, timber processing, tourist activities etc. 6) Delivering skills of efficient project management.
6	**Klaas-Jan Reincke, Managing Director CPD, Estonia**
	Recommendations: 1. In both regions, but especially in Odessa, support the (bottom-up) establishment of coordination bodies for regional development which have two main tasks: 1) the coordination and pooling of resources and initiatives of regional administration, city administration (Odessa and Chernovtsy), NGOs and key businesses and 2) the facilitation of a discussion (rather than an academic analysis) among the key stakeholders on what the main, real priorities for the development of the region are as well as on how, in practical terms, to deliver a regional development strategy based on these priorities. This might involve supporting the central government in creating the legal basis for such organisations, although this would be a longer-term and less straight-forward mission. 2. Provide TA to the strengthening of the initiatives already taken locally to set up credit unions (mainly in Chernovtsy) and – if the fundamentals of such associations prove sufficient – support them financially, possibly complemented by local advisory services to farmers; 3. Support investments in infrastructure to mitigate the risks of flooding damaging the Chernovtsy region´s agricultural production; 4. Support – in cooperation and consultation with DG AIDCO and the Regional Capacity Building Initiative – a more robust training programme for potential applicants from both Chernovtsy and Odessa oblasts aiming to increase their capacity to make use of ENPI-CBC programme funding.

4.2. Wider Recommendations

1. Building on the momentum created by the signature of the MoU and this peer assessment, it is critical that the next steps in the cooperation dialogue be implemented as soon as possible. Logically, a continuation of broad regional development analysis, in the guise of the planned OECD territorial review would be optimal. As the planned OECD territorial review utilises an established international framework and has a proven international validity, the review would prove to be an important step in wider regional development planning, proceeding with this review as soon as possible is critical. In addition, the participation of additional donors in the process would provide additional strategic depth and assist in the process of wider consensus of regional and territorial development. Securing requisite financial resources from national or other donor sources is very important.

2. **Analysis for Growth Opportunities and Regional Competitiveness:** Building on the aforementioned territorial review, a more targeted and comprehensive process

would further extend regional development planning efforts. The regions (Chernovtsy and Odessa – although the issue is the same across all regions) desperately require a targeted strategic focus and direction in broad economic development. They also require effective support to assist in the determination of effective opportunities and where best to channel any resources (albeit limited). An effective regional strategy document which is focused on tangible economic development actions is therefore critical.

As a start to the process a targeted assessment at the regional level (Oblast), utilising a common framework acceptable by all donors and the national government (utilisation of a World Bank or OECD framework would be optimal and provide a common and generally acceptable framework) is critical to provide a clear framework and base on which to develop a system of strategic and policy documents required for regional development. Such a framework assessment would examine:

- Opportunities and constraints for economic Growth (regional level)
- Economic Opportunities through an examination of regional core competence and provision of assistance to develop these competences
- Effectiveness of programmes to support economic development (both national and donor), and the design of optimal programmes/projects to support economic development.

This assessment should be ultimately conducted in all 27 Oblasts (25 Oblasts and 2 cities of Oblast significance), although assessments may start with a workable number of pilot oblasts (4-5) and require a minimum of 2 weeks input of a team to focus on Institution al development, economic opportunities and infrastructure.

3. **Institutional Development:** Institutional development to effectively implement regional development is critical. Currently, no effective coordination body to coordinate the multiple facets of regional development exists in the regions. The bodies involved in regional development represent a wide spectrum of structures (NGO, Oblast Regional Administration, Oblast Councils, Municipalities, individuals), these rarely speak with one voice and appear to be driven by individual self interest of the individual entities (or more correctly the individuals behind these entities). In addition, a significant number of actions related to regional development are driven from the centre, which retains a majority of financial and regulatory control.

   While expending resources strengthening existing institutions is an option, a more effective action may involve supporting the (bottom-up) establishment of coordination bodies for regional development which have two main tasks: 1) the coordination and pooling of resources and initiatives of regional administration, city administration (Odessa and Chernovtsy), NGOs and key businesses and 2) the facilitation of a discussion (rather than an academic analysis) among the key stakeholders on what the main, real priorities for the development of the region are as well as on how, in practical terms, to deliver a regional development strategy based on these priorities. This might involve supporting the central

government in creating the legal basis for such organisations, although this would be a longer-term and less straight-forward mission.

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5. List of Annexes

- Annex A – List of Indicative Questions for Peer Review Workshops
- Annex B – List of Participants – Chernovtsy
- Annex C – List of Participants – Odessa

Annex A- List of Indicative Questions for Peer Review Workshop

A) Danube Strategy and its possible impact on environmental, economic and wider regional development (Odessa only)

How does the Danube Strategy impact on wider regional development in Odessa? What potential positive and negative components are included? Which additional components or considerations would you add to maximize impact of the strategy?

B) Regional Development Structures and Mechanisms - Impact on Regional Development (Constraints and Opportunities)

Who are the key actors/structures in Regional Development policy formulation and implementation? Are these predominately State or non-state actors? What mechanisms exist to balance the interests of diverse interest groups to overcome political economy constraints for coherent regional development policy formulation and implementation?

What is the role (functions) of the Regional Development Agencies in regional development planning and implementation? Which other structures do similar functions? To what degree is their overlap in functions?

How are views from the private sector and civil society taken into account in the wider regional development process and what role do they play in the policy-making process?

What procedures (reporting, benchmarks, etc.) are in place to monitor the effectiveness of institutional structures/RD Programmes?

In your opinion have does the region have adequate capacity to stimulate and maintain effective regional development? What outstanding requirements exist to enhance existing capacity?

C) Economic Development and Competitiveness (Constraints and Opportunities) and its effect on wider regional development

What are the main components of economic activity in your region? Has economic activity in these areas expanded or contracted in the last 10 years? Which new areas of economic activity have emerged in the last years? Which under-resourced or ignored areas do you believe would be economically possible given your experience?

What are the main constraints to economic development in your region?

What are the main competitive advantages (which natural or other resources provide the greatest possibility for future developments). Is competitiveness a major consideration in state and non-state actors in your region?

D) Priorities for regional development in Odessa/Chernovtsy region

What priorities have been elaborated for the development of Odessa/Chernovtsy Oblast. When were these elaborated and what is the status/progress towards their implementation? Which other priorities, in your opinion, have been overlooked or omitted.

E) Impact of financial crisis on regional development

How has the recent financial crisis of the last 18 months affected your region? Has there been a discernable economic contraction? Expansion? Neutral effect? Please elaborate, if you can.

F) Other questions and issues for discussion

Impact and effectiveness of past technical and financial assistance on regional development: Which TA programmes have been implemented in your region in the past 5 years. In your opinion which programmes have been effective? Why? What is the input of regional actors in the planning/allocation of Aid (especially in regional development) and what are the main donors and which sector do they operate?

Annex B- List of Participants – Chernovtsy

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Annex C: List of Participants - Odessa

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