

Ukrainian metallurgy: the economic link in the oligarchic power system

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Theses

1. The metallurgic sector, like the east-west transit of energy raw materials, is a strategic source of revenue for Ukraine. Over the last ten years, this sector has become Kiev's most important source of foreign currency inflows, accounting for over 40 per cent of its total export revenues. The growth of metallurgic production, which has continued almost without interruption since the mid-1990s, has contributed considerably to the increase in GDP which Ukraine showed in 2000, for the first time in its independent history.

2. The sector's economic results improved over recent years in spite of the crisis affecting the machine building industry (including the armaments industry), the traditional buyer of metallurgic goods. The success of Ukraine's metallurgy sector resulted from the relatively favourable overseas economic situation in the late-1990s and the dynamic growth of exports. An important role was also played by the authorities' policy of granting the metallurgic industry a series of tax rebates in 1999 as part of the so-called economic experiment in the sector. Facing both the decline in the world economic situation and the Ukrainian metallurgy sector's dependence on foreign markets, the authorities in Kiev have chosen to continue their original policy of favouring this sector. The importance of metallurgic exports for Ukraine could be compared to the importance of energy raw material exports for Russia.

3. As this sector of industry is so attractive, owing to its immense export revenues, it has quickly found itself in the hands of new owners, who have usually been affiliated to the enterprises' original managers. Over recent years, local industrial-financial groups (IFGs) have been playing an increasingly important role. The IFGs include such organisations as Industrialnyi Soyuz Donbassa, Metallurhiya or Interpipe, within which the consolidation of the sector's enterprises is taking place. The evolution of the IFGs has followed the model of their Russian counterparts' development, in trying to form conglomerates of establishments with complete, closed production cycles.

4. Even though the presence of Russian investors in local ferrous metallurgy is relatively small, Russia plays a very important role in this sector of Ukraine's economy. It remains an important market for the local metallurgic industry and its key co-operator. As the production volumes of Ukrainian metallurgy grow, the demand

for (and consequently the dependence on) Russian raw materials grows as well. The Ukrainian IFGs doing business in this sector often have no choice but to co-operate with their more potent Russian counterparts.

5. The Ukrainian IFGs, who are now the main investors in the market, are restructuring the enterprises that they control – but too slowly, thus failing to meet the entire sector's needs. Also, this restructuring first and foremost consists in investments in those undertakings which export their products. Meanwhile, degradation of production potential is progressing in line with technological obsolescence, and the gap between the sector and its foreign competitors is widening. Consequently, the industry calls for enormous investments. The transformation model implemented so far, and the conservative policy of the state, seem to form a strategy of half-measures, which impedes deeper reforms and blocks the influx of foreign investments.

6. Each major IFG has its own political backup in the authorities at regional or national level, depending on the scale of its investments. In recent years, the symbiosis of the political and business portions of the IFGs has brought about rises and falls of particular business empires, as their respective political patrons ascended to power and then lost it. Metallurgy being the basic source of economic and political influence in Ukraine, the model of development that the sector has been implementing so far has contributed to the maintenance of the oligarchic political and economic system in Ukraine.

1. The importance of metallurgy for Ukraine's economy

The development of the metallurgical industry in Ukraine dates back to the 19th century, when numerous deposits of iron ore and coal were discovered. This was associated with the accelerated economic development taking place in tsarist Russia at the turn of the 20th century. The former empty expanses in south-east Ukraine underwent rapid urbanisation and industrialisation. The shape of subsequent Soviet investments in Ukraine's metallurgy was determined by the fact that Ukraine was one of the only three Soviet republics that had large deposits of iron ore, the other two being Russia and Kazakhstan. Heavy industry in the USSR was developed rapidly; this led to the further industrialisation of

Ukraine, which became the USSR's leading industrial centre, as well as its 'granary', and developed a ferrous metallurgy potential that was comparable to that of Russia¹.

The break-up of the USSR gave rise to deep recession, and brought about changes in the structure of the former Soviet republics' industry. It also caused a breakdown of trade between the countries of the Commonwealth of Independent States. This resulted in a dramatic decline in demand for steel products. Due to the drop in both domestic sales and sales to the traditional CIS markets, the output of steel products began to decrease, which process continued in Ukraine until the mid-1990s². As a result of the decline in goods trade within the CIS, its member countries reoriented their exports and found new foreign markets in other countries.

The output of Ukrainian metallurgy has been growing since 1996, this growth being disturbed only once in 1998, when the ferrous metallurgy sector showed a decline of nearly 7 per cent. The results for 2000 were particularly impressive: ferrous metallurgy output increased by 20.7 per cent and the output of non-ferrous metallurgy grew 18.8 per cent, these figures being much higher than the production growth indexes for industry in general (12.9 per cent). Preliminary data show that production output continued to grow in 2001, although in the second half of the year the dynamics of this growth slowed down. According to the International Iron and Steel Institute (IISI), in 2000 (as in 1999) Ukraine was the world's 7th largest steel producer³.

These figures improved despite the crisis affecting the machine building industry and the armaments industry, the basic consumers of metallurgical products, which continued until the late 1990s. This was possible owing to a systematic growth in exports, which took advantage of the favourable pricing situation in the world at that time. Conditions for exports improved further following the devaluation of the Ukrainian currency after the 1998 financial crisis. The policy of favouring the metallurgical sector implemented by Kiev also played a role in the growth in exports. Exports account for a dominant portion (about 80 per cent) of the Ukrainian metallurgical sector's total sales. This structure is a reversal of the sales structure of other leading metallurgical producers. In the 1990s, sales to various countries of the world grew at the expense of supplies to the CIS markets⁴. The main directions of expansion (as in the case of other producers from the CIS) included the Middle East, Latin America and countries in Asia and Africa. These destinations accept about 70 per cent of

Ukrainian metallurgy's exports. Apart from finished rolled products (pipes, rails, sheet metal, fixtures, profiles and so on) Ukraine exports iron ore, ferroalloys, cast iron, a growing proportion of semi-finished products, and metal scrap. According to the IISI, in 2000, Ukraine was the world's fifth largest exporter of steel products, and (due to its scarce imports) the third largest net exporter after Russia and Japan⁵. Due to the increased volumes of exports and the dynamic growth of production, the share of ferrous and non-ferrous metallurgy in the total value of industrial production grew three times over the last decade, from 12.1 to nearly 30 per cent. In 2000, the dynamic growth of industrial production, which increased 12.9 per cent, contributed to the first increase in GDP in the history of independent Ukraine.

The metallurgic sector in Ukraine comprises several hundred enterprises, including 14 steelworks, 7 pipe factories, metal plants, iron ore production and enrichment plants, 3 ferroalloy establishments, 16 coke processing plants, 20 non-ferrous metallurgy plants and 35 plants dealing with secondary metallurgy of iron and non-ferrous metals⁶. These industrial establishments, especially the non-ferrous metallurgy plants, are scattered all over the country.

The ferrous metallurgy potential, including the largest establishments, is concentrated in the four South-east oblasts (provinces) of Ukraine. The Dnipropetrovs'k oblast produces over 80 per cent of the country's iron ore, the basic raw material for steelmaking. The other necessary raw material, coke, is produced mainly in the Donets'k oblast, and in the country's largest mining and metallurgic complex in Kryvyi Rih (the Dnipropetrovs'k oblast). Almost 100 per cent of Ukraine's steel is produced in the following districts: the Donets'k oblast (14 million tons, i.e. over 44 per cent of total domestic production), the Dnipropetrovs'k oblast (10.2 million tons, i.e. 32.2 per cent), the Zaporizhia oblast (4.4 million tons, i.e. 14 per cent) and the Luhans'k oblast (2.9 million tons, i.e. 9 per cent). Most steel (about 70 per cent) is produced by the following industrial complexes: Kryvorizhstal of Kryvyi Rih, the Mariupol Illich MMK and Azovstal (Donets'k oblast), Zaporizhstal of Zaporizhia (Zaporizhia oblast) and AMK of Alchevs'k (Luhans'k oblast). The production of cast iron and rolled steel products is also concentrated in these districts, as well as in the so-called 'great five' steelworks⁷. These five establishments are included in the list of the world's eighty largest producers of steel for 2000 as compiled by the IISI⁸. The production of pipes is concentrated in the Dnipropetrovs'k oblast, where four of Ukraine's seven factories are located.

Companies from the metallurgic sector lead the rankings of Ukrainian enterprises, which is published each year by the *Ukrainskaya Investitsionnaya Gazeta weekly*. Among the top 100 enterprises with the highest incomes in 2000, 24 were establishments from the metallurgy sector, in addition to a further dozen or so intermediaries that trade metallurgic products. In the top ten, as many as six entities were associated with metallurgy. The importance of the metallurgic sector is illustrated even better by the ranking of top exporters. In the top ten, there is only one company not directly associated with metallurgy⁹.

The proportion of metallurgic exports in Ukraine's total exports is comparable to the proportion of its energy raw materials imports in total imports. The value of the 2000 imports of the so-called 'mineral products', which include Russian gas and oil, exceeded US\$6.5 billion and accounted for about 47 per cent of the total value of goods imports. On the other hand, Ukraine's exports of metals and metal products generated revenues of about US\$6.5 billion, which accounted for as much as 44.4 per cent of total export revenues. The proceeds from metallurgic exports exceed Ukraine's total income from transit services (nearly US\$3.5 billion in 2000), including the transit of gas and oil (nearly US\$2 billion)¹⁰. In recent years, it has been proved that metallurgic exports are not only the motor of Ukraine's entire economy, which is focused around heavy industry, but also the main source of foreign currency proceeds. For Ukraine, the importance of metallurgy is comparable to the importance of energy raw materials for Russia.

2. Metallurgy – the economic link in the oligarchic power system

Metallurgy is one of the basic sources of economic influence, and consequently of political power, in Ukraine. The model of development which the sector has been implementing so far reflects the development of the oligarchic political and economic system that has been forming in Ukraine since the early 1990s.

The main entities around which the sector is consolidating are the Ukrainian interest groups frequently referred to as industrial-financial groups (IFG)¹¹. These groups' expansion is conditioned by political protectionism, the scope of which corresponds to the scale of individual IFGs' investments. This protectionism gives the IFGs a privileged position in relation to foreign investors. This

is their basic asset in their rivalry with Russian capital, but at the same time it is one of the fundamental barriers that impede major Western investments.

The first Ukrainian IFGs began to form back in the early 1990s. For many of them, the basic capital necessary for development turned out to be not finance per se but rather 'assets', such as the power to influence the authorities, from the managers of particular state-owned enterprises to the regional authorities (who shape the economic and political lives of the Ukrainian provinces), and to the political elites in Kiev. As a result of this symbiosis between political power in the state and economic power in the economy (especially in metallurgy), many leading IFGs have risen and fallen in recent years as their political patrons gained and lost power.

The political backup of the largest Ukrainian IFGs includes the highest state authorities. One example of this is the United Energy Systems of Ukraine (UESU) corporation, which was promoted from 1996 to 1997 by then Prime Minister Pavlo Lazarenko. It is typical that in addition to making business investments, particular IFGs have 'invested' in political parties and parliamentary factions. 'We say Hromada, we think UESU', wrote the Kiev press four years ago, referring to the links that existed between the party chaired by Pavlo Lazarenko and the then most potent private commercial organisation in Ukraine¹². Trubova Ukraina ['Pipe Ukraine'] was the spiteful nickname of Trudova Ukraina, the second largest parliamentary faction (after the communists) in the Verkhovna Rada of the previous term (1998–2002), which was associated with the steel pipe trader Interpipe. The political and business environment of the group, which was affiliated to the Social-Democratic Party of Ukraine (United) and which invested in a number of industries, including metallurgy, is sometimes referred to as the Social Democratic Holding.

The scope of these political and business formations' influence in the state is very broad, and is not limited to politics or the economy (and in the economy, it is not limited to metallurgy). The IFGs' owners and political patrons are commonly referred to as oligarchs, as in Russia. They control the largest media, which are in a way 'cursed' to dependence on such investors owing to the economic weakness of the state and the narrowness of the advertising market (this being one of the main barriers that impede the development of independent media in the post-Soviet area). The media serve their owners by lobbying for economic projects profitable for the latter, and they serve the IFGs' political protectors by promoting their political strategies. The evolution of

the Ukrainian IFGs has followed the pattern of their Russian counterparts' development, although the process is slightly retarded. The importance of these political-business formations in Ukraine, which are characteristic of nearly the entire post-Soviet area, is comparable to the role that the Russian IFGs played during Boris Yeltsin's presidency. This model of development strengthens the oligarchic system of power and retards reforms in the state.

As the publicist Aleksandr Menshakov figuratively put it, the oligarchisation of the state on the regional level consists in the formation of specific tiny 'Soviet Socialist Republics'. Such 'SSRs', managed jointly by the local administration and skilful economy specialists who know how to evade taxes and profit their corporations, take control over more and more enterprises. Directors of state-owned enterprises receive tempting proposals to co-operate with certain selected companies. If they accept these proposals they keep their positions, but if not, they quit – in one way or another. In this model, enterprises of entire regions function within certain corporations. It is unimportant, Menshakov argues, which establishments have already been privatised and which have not; the privatised gets to be controlled by publicly unknown shareholders (usually through 'foreign' companies with exotic names, incorporated in equally exotic countries), and the state-owned company starts to be managed by directors appointed by the local clans and the IFGs associated with such clans. 'It is obvious that no economic entity, after having undergone this kind of 'privatisation', will ever seriously participate in the market auctions for coal or gas, in any other tenders or in the market commercial exchange in general. What to sell or buy, how, or for what price – all this will be dictated by some Gosplan of the regional business-political structure(...)'¹³.

2.1. The Donets'k Group: Industrialnyi Soyuz Donbassa

For the Ukrainian publicist, a model example of a 'regional' IFG¹⁴ is Industrial Union of Donbass Corporation (IUD), the business link of the so-called Donets'k clan, that is, a specific political-business corporation which has gained control of the Donets'k oblast (province), and is slowly expanding into other parts of Ukraine. The expansion of the Donets'k elite is linked to the region's economic potential (the region produces over fifty percent of the country's coal and nearly fifty percent of its coke and steel¹⁵). It even 'elevated' Yuhym Zviahivskyi, one of the local leaders, to the position of acting Prime Minister of Ukraine in autumn 1993. But

the competing Dnipropetrovs'k clan soon reclaimed power in the state. Changes at the top in Kiev brought about Zviahil'skiy's rapid resignation (1994), and he had to flee to Israel in an atmosphere of scandal¹⁶. The political ambitions of the Donets'k group were curbed, and their activities were restricted to the regional level. Since the mid-1990s, the Donets'k political-business elite has been acting in line with the slogan 'politics is done in Kiev, and business in the Donbass'¹⁷. This policy has manifested itself in the group's unconditional political support for President Leonid Kuchma. In return, the group has received an almost unlimited right to carry out economic expansion in the region.

As part of this expansion, between late 1995 and early 1996, the Industrial Union of Donbass (IUD) corporation was established with the 'blessing' of the oblast's authorities. In 1996, Volodymyr Scherban', the then governor of the Donets'k oblast, ordered the industrial establishments of the region to break their relations with all gas suppliers except for IUD. The latter soon became the region's new gas monopoly. IUD initially profited from the supplies of Russian gas and settlements with the industrial gas consumers (each year, the Donets'k district consumes a quantity of gas comparable to the total gas consumption in Poland). In this way, Governor Scherban' was acting to the disadvantage of the inter-regional UESU corporation favoured by Prime Minister Pavlo Lazarenko¹⁸. Scherban' was soon dismissed, and many representatives of the Donets'k business-political elites died in unclear circumstances¹⁹. However, the expansion of UESU was stopped following President Kuchma's unexpected dismissal of Prime Minister Lazarenko in 1997²⁰. The Donets'k governor's seat was offered to Viktor Yanukovych who is associated with the businessman Rinat Akhmetov who became the new informal leader of the clan²¹. Since that time, the IUD has taken control over ever more enterprises, including Azovstal, the country's third largest metallurgic complex. According to the Ukrainian press, it controls over 600 enterprises in the Donets'k and Luhans'k districts at the moment²². Very often, the bonds between IUD and the enterprises it controls are informal. Khartsyzsk Tube Works

IUD is very confident in its relations with enterprises it does not formally own. This may be attested by the concern's investments in the modernisation of production lines at the pipe factory in Khartsyz'k (Khartsyzsk Tube Works, KTW) in the period preceding its privatisation²³. As a result of this co-operation, in September 2001 IUD formally took over control of KTW, a CIS-area monopolist manufacturer of large-diameter (530–1420 mm) pipes with anti-corrosion coating necessary in pipeline construction.

IUD won the privatisation competition by offering 126 million hryvnas (about US\$25m), i.e. only 3 million hryvnas above the upset price (and over 200 million hryvnas below the upset price quoted in the first failed attempt to privatise KTW in 2000). With over 6 billion hryvnas of revenues (over US\$1 billion), IUD is Ukraine's second largest enterprise after the Naftohaz Ukrainy complex²⁴. The annual revenues of its partner companies (sometimes taken to be IUD 'affiliates'), such as ARS, Danko or Donets'kyi Industrialnyi Soyuz, account for another 8 billion hryvnas. For comparison, the 2000 GDP of Ukraine in current prices amounted to about 173 billion hryvnas²⁵. In 2000, IUD exported products worth US\$363m, which puts it fourth in the ranking of Ukraine's largest exporters²⁶.

One of IUD's founders is Vitaly Haiduk, who was appointed Minister of the Power Sector towards the end of 2001. Shortly after taking office, Haiduk objected against the creditors' attempts to file a petition in bankruptcy against the Dniiproenerho energy plant. Dniiproenerho is one of the entities that buy the gas traded by IUD. Haiduk also suggested a reduction in energy prices for the key sectors of the economy; this just three days after his superior, Prime Minister Anatoly Kinakh, signed a regulation to increase prices for industrial customers²⁷. Haiduk said that he did not know anything about the regulation, and even if it actually had been signed, he did not support it [sic]. The next day, the Prime Minister confirmed that the regulation had been passed, but a day later President Leonid Kuchma ordered the government to consider the idea of creating 'an integrated fuel and energy organisation for Donets'k' within which prices would be fixed on special terms²⁸. This example of relations between the Prime Minister and his subordinate, and of the President's subsequent reaction, well illustrates the way in which the Ukrainian government functions. It also shows how the Donets'k group's position in Kiev strengthened in 2001.

The 'political pragmatism' of the Donets'k group is demonstrated by the fact that the Regions Party, which represents the group, is a member of the pro-presidential, *nomenklatura* and oligarchic 'Za Yedynu Ukrainu' [One Ukraine] coalition formed for the 2002 parliamentary elections. Among other members, this coalition includes the Trudova Ukraina party, which is affiliated to the Interpipe group, which is in turn a business competitor of IUD.

2.2. The Dnipropetrovs'k Group: UESU, Interpipe, Pryvatbank

In the 1990s, the Donets'k clan lost the battle for power in Kiev to the elites of another important Ukrainian economic centre, the Dnipropetrovs'k oblast. The importance of Dnipropetrovs'k in Ukraine dates back to the Soviet period, when the giant establishments of the Soviet armaments and space industry were created there. The local *nomenklatura* was responsible for these sectors, which were of key importance for the Soviet state. It administered them on behalf of Moscow, rather than Kiev, which had an impact on both Dnipropetrovs'k's importance in the USSR (Leonid Brezhnev, among others, came from this district), and the prospects for its development in independent Ukraine. Owing to its more comprehensive experience, the Dnipropetrovs'k group proved better prepared to take power in Kiev than the Donets'k elite, which had been focused on the mining and metallurgy 'monoculture' of the Donbass.

A number of Ukraine's leading contemporary politicians come from Dnipropetrovs'k, starting with President Leonid Kuchma himself (who used to be a member of the management team of Pivdenmash, the world's largest space rocket factory²⁹), to ex-Prime Minister Pavlo Lazarenko (1996-7), former Deputy Prime Minister Yulia Tymoshenko (2000), and to the influential deputies Viktor Pinchuk and Serhiy Tyhybko. The Dnipropetrovs'k elites, though, do not form a monolith like the Donets'k group. Following the Dnipropetrovs'k group's expansion in the 1990s, several circles of influence emerged around the most effectual and ambitious representatives of the local clan.

The Lazarenko-Tymoshenko duo created the United Energy Systems of Ukraine (UESU) concern, an interregional IFG which is currently Ukraine's largest. It was established back in the mid-1990s on the foundation provided by the Dnipropetrovs'k 'family business' of the Tymoshenko family, the Ukrains'kyi Benzyn corporation³⁰. In 1996-7, UESU controlled the most important sectors of the economy and did business on a massive scale. Its operations were not restricted to the territory of Ukraine, as is evidenced by the numerous investigation proceedings pending in Moscow and other places, which pertain to suspected transactions worth hundreds of millions of dollars, and involving Gazprom and the Russian defence department. According to some sources, when UESU's power was at its peak (1997) the corporation controlled a quarter of Ukraine's economy³¹. UESU thrived on the protection provided by the Prime Minister as well as

the barter settlement schemes under lucrative gas supply contracts (UESU briefly became Ukraine's single largest private gas importer). The successes ended with the fall of Pavlo Lazarenko's government. At the moment, UESU is in a deep defensive position, as are the creators of its power³². The remnants of the former empire, including its metallurgic assets, are gradually being taken over by Yulia Tymoshenko's political and business competitors. An example: until recently, the group's companies controlled the leading iron ore production and enrichment complex, the Pivdennyi HZK in Kryvyi Rih. In summer 2001, three companies from the UESU group (Lanata Trading, Lansin Commercial LTD and Doleno Trading LTD, all registered in tax havens) which jointly controlled over 60 per cent of HZK shares, were to be sold for about US\$50m to Russia's LUKoil. But the Pryvatbank group struck back with the assistance of the courts, and ultimately the future of HZK remained unresolved³³. In 2001 the Slovianskyi bank, which had developed dynamically in the 1990s and formed an important link in the IFG, was put into liquidation³⁴. The history of the expansion and fall of UESU and its political promoters is a perfect illustration of the interdependence of Ukraine's economy and politics.

The ruins of UESU served as a foundation for the now leading Ukrainian IFG, the Interpipe group. There is a special link between its owner Viktor Pinchuk (one of the leaders of the Trudova Ukraina parliamentary faction) and President Leonid Kuchma: Pinchuk is the second husband of the President's daughter, Olena Franchuk (Franchuk being the name of her first husband, son of the former Prime Minister of the Autonomous Republic of Crimea). For quite some time Pinchuk has been considered to be the most influential oligarch in Kuchma's inner circle, a member of the so-called Family (modelled on the Moscow 'Family' that formed around former Russian President Boris Yeltsin)

Interpipe was established back in 1990, but the period of its particularly rapid expansion followed Lazarenko's political crash and UESU's economic breakdown. Interpipe gained control of a number of Eastern Ukrainian enterprises in 1999, the year of the last presidential elections, during which Pinchuk's media empire (which owns the country's leading television, the ISTV, and *Fakty i Kommentarii*, one of the largest national dailies) became one of the main sponsors of Leonid Kuchma's presidential campaign³⁵. Even though Pinchuk's concern lost the battle for the CIS' key-importance pipe factory in Khartsyz'k to the Donets'k IUD in 2001, Interpipe's business thrives on the manufacture and export of steel pipes. The concern controls most domestic pipe facto-

ries, which are concentrated in the Dnipropetrovs'k district (like the Nizhnedniprovsky Truboprotkatny Zavod or the plants in Novomoskovsk and Nikopol; in the course of restructurisation, the latter one was transformed into a new enterprise named Niko-Tube, which is now part of Interpipe). Interpipe also controls some establishments in other CIS countries (including the plants in the Belorussian Mogilev district). Dnipropetrovs'k is the seat of the Kredyt-Dnipro bank, which is the group's financial link. Interpipe sells most of its products to countries in the CIS and Central and Eastern Europe, the rest being sold to Western Europe, America and Asia³⁶. Through Kredyt-Dnipro, the group controls the Nikopol Ferroalloy Plants, one of three such establishments in Ukraine, as well as other enterprises. In 2000, Interpipe had the tenth highest total revenues among Ukrainian companies (2.7 billion hryvnas or over US\$500m in revenues; it was just behind the national telecom operator, Ukrtelekom), the fifth biggest exporter (just behind IUD at US\$237m) and twenty-third in the ranking of the most profitable companies (104 million hryvnas, i.e. about US\$20m)³⁷.

The Pryvatbank group is another important Ukrainian IFG with its origins in Dnipropetrovs'k. The Pryvatbank and Interpipe groups have more in common than their geographic origin, though, as they are also affiliated in political and business terms. Companies of the Pryvatbank group, like the other leading IFGs of Ukraine, invest in various sectors of the economy; the most important directions of their expansion include ferrous and non-ferrous metallurgy. The Pryvatbank IFG is concentrated around Ukraine's leading private bank, AKB Pryvatbank, which was established by other major entities of the group, namely Privat Intertrading and Sentoza. It owes a lot to former Vice Prime Minister Serhiy Tyhybko, an opponent of Yulia Tymoshenko and an ally of Viktor Pinchuk. In 2000, Tyhybko was a member of the 'reformers' cabinet' of Viktor Yushchenko, but as a result of the disputes around Deputy Prime Minister Tymoshenko's energy policy, Tyhybko resigned from the position of the Minister of Economy and quit the government after several months. At that time, he became one of Tymoshenko's main opponent and was shortly elected chairman of Pinchuk's party, i.e. *Trudova Ukraina*³⁸. In this context it is hardly surprising that the Pryvatbank group's companies struggled with the structures affiliated to Yulia Tymoshenko for one of Ukraine's largest ore enrichment plants, the Pivdenniy HZK in Kryvyi Rih.

2.3. The Social-Democratic holding

In 2000, a new fundamental requirement was introduced into the privatisation procedure, namely the criterion of the so-called industry investor with adequate experience and background in the given industry. This was why the Metallurhia concern was established in early 2000 for the purpose of taking part in the privatisation process. It represented the interests of a business group associated with Hryhoriy Surkis, one of the leaders of the Social-Democratic Party of Ukraine (United) (SDPU(o)). Surkis was also a political and business partner of Viktor Medvedchuk, who until shortly before had been vice-chairman of the Parliament. However, this group's metallurgy holdings are less extensive than the assets of IUD, and are expanding less dynamically than the Donets'k group and Interpipe have been doing recently.

The *Social-Democratic holding*, as the political and business environment of Surkis, Medvedchuk and the SDPU(o) is sometimes called, began its expansion into the fuel sector with the Slavutych concern. Its main industrial assets include the Zaporizhia Ferroalloys Plants, the Dneprospetstal complex³⁹ and a chain of regional energy enterprises.

The 'Social Democrats' own one of the most potent media empires in Ukraine. Among other establishments, they control Inter television, and influence Studio 1+1 (the two most popular stations in Ukraine), as well as the popular capital city daily *Kievskiy Vedomosti*. The media associated with this group have been carrying out an incessant defamation campaign against Viktor Yushchenko for nearly two years. Yushchenko exposed himself to the 'Social Democrats' displeasure in 2000, when as the government's Prime Minister he undertook reforms in the energy sector, then partly controlled by structures associated with SDPU(o). The SDPU(o)'s political position has been unstable recently, which has manifested itself in the distance that formed between the 'Social Democrats' and the President's formation, and in Viktor Medvedchuk's dismissal from the position of vice-chairman of the Parliament. This does not bode well for the potential future expansion of the Social-Democratic holding. The results of the spring elections to the Verkhovna Rada may strengthen or weaken particular groups of economic influence.

2.4. The state's policy towards the sector

The state's policy towards the metallurgy sector is notable for the implementation of the half-measures characteristic of Ukrainian reforms in general. One such half-measure was the so-called tax experiment in the sector. Previously, the state's policy of supporting the metallurgy sector was not much different from its policies towards other sectors. It included the practice of redeeming the enterprises' debts, while the state itself simultaneously failed to regularly meet its own obligations towards metallurgy; one example of this is the postponement of implementing a comprehensive solution to the issue of VAT reimbursement to exporters, mostly from the metallurgy sector.

The law 'On the performance of an experiment in the metallurgic sector enterprises' became effective on 1 July 1999. It provided for a number of tax breaks and privileges for a selected number (67) of steelworks, mines, ore enrichment plants, pipe factories and so on. These measures were to remain in force until the end of 2001. The establishments included in the experiment enjoyed reduced profit tax rates (down to 9% in the first year and 15% in subsequent years), reduced ecological charges (down to no more than 0.15 per cent of their foreign currency expenditure), redeemed fines for untimely payment of dues and taxes, and reduced fine rates and contributions to the National Innovation Fund by half. The 'experimental' companies were also exempted from charges for the construction, overhauls and maintenance of roads⁴⁰.

The sector's situation improved considerably thanks to the tax rebates, and one of the experiment's objectives was attained, namely the financial liquidity and an improvement in the quality of settlements in the sector (which, however, also resulted from other economic reforms undertaken in 2000 aimed at limiting the use of barter). The state's total aid provided to the sector in 1999 and 2000, including rebates, redemption of fines, deferment of tax payments etc., reached over 4.5 billion hryvnas (nearly US\$900m)⁴¹. As the volume of production increased dynamically in the first phase of the experiment, the sector's payments to the budget began to increase. This continued until 2001 when, according to Ukraine's Tax Administration, many enterprises began to show losses⁴².

The lobby associated with the major IFGs managed to extend the duration of the experiment by pointing to the deteriorating economic situation. On January 17, the Verkhovna Rada extended the

validity of the experiment law until the end of 2002⁴³. Opponents have criticised the experiment as an example of unequal treatment of economic entities and a threat to the budget. They have also been arguing that extension of the experiment may cost the budget 1 billion hryvnas (about US\$200m), which amount will be spent on the electoral campaign. Among other problems, this argument refers to the fact that most enterprises in the sector are controlled by the same industrial-financial groups which are affiliated to the pro-presidential *Za Edinu Ukrainu* electoral coalition.

3. Foreign investment

The authorities' inconsistent economic policy, non-transparent privatisation and a brand of protectionism that favours selected domestic industrial-financial groups are barriers that deter serious foreign capital, and Western capital in particular, from investing in Ukraine's metallurgy sector. Foreign capital has so far been committed mainly to non-ferrous metallurgy and to smaller enterprises. In most cases, this commitment consists in the use of local production resources on a tolling basis⁴⁴. The only real investors are the Russians, even though their commitment in the metallurgy sector is relatively small compared to other sectors of the Ukrainian economy (petroleum refinery in particular), and focuses on non-ferrous metallurgy.

In March 2000, the Russky Alumini concern, acting through its Ukrainian company, won the privatisation of the Mykolaiv Aluminosilicate Plants that produces aluminosilicates, a semi-finished product necessary for the production of aluminium, and which is scarce in the CIS. The Russians, who had previously held a block of shares, paid over US\$100 million – a record amount in the history of Ukrainian privatisation – for the 30 per cent block of the state's shares in the enterprise which they needed to control it. A year later, 68.01 per cent of shares in Ukraine's only aluminium plant in Zaporizhia (ZZA) were purchased by Russia's AvtoVAZ-Invest, a company associated with the automotive concern in Togliatti – an entity which was naturally interested in the ZZA's products. The only major Russian investment in ferrous metallurgy was the takeover of the middle-size steelworks in Donetsk by Metalsrussia⁴⁵. The real scope of the Russians' commitment in Ukraine's metallurgy sector is undoubtedly higher, but at the same time it is difficult to verify because of the insufficient transparency of ownership issues in Ukraine⁴⁶.

The Russians' capital commitments on the one hand, and the key importance of Russia for Ukraine's metallurgy on the other, are largely a legacy of the joint economic organism of the USSR and the co-operational bonds that existed between enterprises of both states (only 20 per cent of Ukrainian enterprises have production cycles that are closed within the republic's limits⁴⁷). Russia remains the most important market for the Ukrainian producers of the aluminosilicates necessary to produce aluminium, steel pipes for the construction of gas and oil pipelines, etc. At the same time Russia is the main supplier of gas, the importance of which increases as production volumes in Ukraine grow (metallurgy and the energy sector consume the largest quantities of this fuel).

Russia is also important from the point of view of the leading Ukrainian industrial-financial groups' expansion, as their further development is conditional not only on exports to the Eastern market (as in the case of Interpipe), but also on joint Ukrainian-Russian undertakings, including undertakings in third countries (for example, IUD is an important partner for Russia's Gazprom as the main supplier of metal products for Gazprom's deposit preparation project in the Persian Gulf⁴⁸).

4. Principal developments and future prospects

For several years, Ukraine has been consistently taking measures to re-attain the level of metallurgy outputs from the Soviet period. The growth in the metallurgy sector's production has considerably contributed to the improvement of the entire economy's results. However, this growth was founded on the favourable economic situation in foreign markets and the Kiev authorities' policy of favouring the sector, rather than on structural reforms in the industry. Meanwhile, the successful development of exports also has negative aspects.

The relation between domestic sales and sales in the foreign markets is about 20 per cent to 80 per cent. The slight increase in internal demand observed in 2000–2001 will not be enough to compensate for the overseas markets. According to optimistic forecasts, by 2010 the Ukrainian market will be able to absorb up to 8 million tons of rolled products, i.e. as little as 35 per cent of the present production volume. Because of such a deep dependence on exports, Ukraine will remain exposed for many years to fluctuations in the world economic situation which will affect the volume of investments in the sector, GDP growth and the condi-

tion of Ukraine's budget. In 2002, the export conditions for the Ukrainian metallurgy enterprises will worsen. The declining economic situation abroad will be combined with the prospect of increased costs, owing to the expected growth of internal market prices of gas, electricity, etc.

In the face of symptoms of a world-wide recession, which intensified after 11 September 2001, the largest steel producers concluded an initial agreement in December last year to reduce their production resources by 10 per cent (about 100 million tons) by 2010. Ukraine refused to support this agreement, but it may surely expect difficulties with export, especially of processed products. The developed countries will try to protect their markets from imports; this has already manifested itself in the decisions taken by the US and EU in early spring 2002 to protect their respective markets, the restrictions Russia imposed last year on the import of Ukrainian steel pipes, and the ever more numerous anti-dumping proceedings initiated against Ukrainian exporters. The structure of Ukrainian exports in terms of proportions of particular goods is especially unfavourable. Between 1995 and 2000, the proportion of cheap, low-processed products such as cast iron and semi-finished products in foreign sales increased, and the proportion of finished rolled products dropped. The trends in the exports of developed countries are just the opposite, as these countries try to sell highly processed, expensive products abroad. By exporting cast iron, Ukraine is supporting its competitors' raw materials base. In the opinion of experts, the competitive advantage which Ukrainian metallurgy has so far enjoyed in the world is precisely the consequence of the low level of processing and low prices of its products.

The potential of Ukraine's metallurgy sector, developed back in the Soviet period, is based on obsolete technologies, which reflected the standards and needs of the extensively developing Soviet economy. This determines the quality of the product Ukrainian metallurgy offers today, as well as the above-mentioned resulting problems in the world markets. According to some estimates, over 60 per cent the Ukrainian metallurgy's output is based on obsolete technologies, and only 62 per cent of Ukrainian metallurgy exports may be certified as complying with international standards⁴⁹.

In 2000, only 3.1 per cent of Ukrainian steel was produced in electrical furnaces, while this modern melt technology accounted for 14.6 per cent of Russian production, and an average 33.8 per cent of world production. Fifty per cent of Ukrainian steel is produced in open-hearth furnaces. This technology accounts for 27.4

per cent of Russia's production, and is almost completely out of use in developed countries. However, there has been a certain improvement: from 1998 to 2000 the proportion of steel produced in the continuous casting system increased from 17.5 to 19.6 per cent. But even so, Ukraine remains far behind its competition in this respect (the continuous casting system accounts for 49.7 per cent of production in Russia and 84.7 per cent of production in the rest of the world)⁵⁰.

The technological obsolescence causes considerable raw material losses in the production process. Ukrainian metallurgy shows higher raw material and energy consumption than the average in developed countries. The consumption of steel per ton of finished rolled products is 1.3 tons, compared to 1.25 tons in Russia, 1.18 tons in the US and 1.05 tons in Japan. The high energy consumption level of most establishments exposes them to problems as the prices of imported energy raw materials increase. The prices of domestic coal and transport are another important factor. These prices, however, are shaped by the state, so the political backup of Ukraine's particular industrial-financial groups plays its role here.

Apart from being a legacy of the USSR's 'moon economy', this technological obsolescence also results from low investments in the sector in the 1990s. Most of the local metallurgic undertakings were established several decades ago, and many even before the Second World War. Broad-scale investments ended with the crisis and break-up of the USSR. The wear and tear of fixed assets in early 2000 reached 63.1 per cent, and each year, amortisation amounts to 3–3.5 billion hryvnas (US\$550–650m); reconstruction expenditures in 2000 amounted to just 1.6 billion hryvnas, and even this was mainly due to the so-called economic experiment in the sector⁵¹. Meanwhile, restructurisation of the sector would require investments at an estimated amount of 40–50 billion hryvnas⁵² (US\$8–10 billion). Such investments could be only afforded by serious Western investors. This prospect, though, appears unrealistic at the moment, because there is no will to fundamentally change the state's economic policy. Besides, most of the sector's enterprises have already been privatised.

The improved results the sector showed in recent years were not due to reforms, but rather to the favourable international economic situation in the late 1990s, and to the policy of the authorities in Kiev who offered the metallurgy sector successive restructurisations of debt and tax abatements instead of a comprehensive development strategy. Owing to these hothouse conditions, the prospects of a deep qualitative change in the sector

are now ill-defined, and the sector's managers are motivated to lobby for the maintenance of the status quo, i.e. for the state's policy of privileging the sector and restricting competition. This was clearly visible in the privatisation process, which was formally 'open' and yet de facto closed to investors from 'outside', especially the West.

In this way, the restructuring and consolidation of Ukraine's metallurgy (which has little in common with the consolidation processes taking place in the world's markets) will continue to take place around the local industrial-financial groups. In such a situation, the large Russian concerns are the only potential foreign investors. The consolidation of this sector is a process similar to the developments taking place in Russia, although it is several years behind. The Ukrainian IFGs are trying to form chains of companies that encompass complete production cycles, and after taking control over particular establishments they make modernisation investments mainly in those which export their products. On the one hand, this reduces the risk of instability of raw material and semi-finished products supplies to the exporting enterprises within the group, but on the other, it leads to restriction of competition in the domestic market, and a widening gap between the levels of modernisation investments in the key enterprises exporting their products (steelworks, pipe factories), and the raw material backend (the extraction industry). The 'extensive' model of the sector's development preserves the outdated structure of an economy oriented towards quantity rather than quality. It also makes this economy strongly dependent on Russia, which remains the most important market for Ukraine's producers and the main source of gas supplies (the importance of which grows in line with the increasing volumes of industrial production in Ukraine⁵³), and is in fact the only real investor in Ukraine. This development model also determines the direction of the oligarchic political and economic system's evolution, as the latter has similar roots and a number of shared characteristics.

The development model which Ukraine's metallurgy sector has been implementing so far and the interdependence of business and the structures of power are serious barriers that impede not only the sector's restructuring, but also reforms to the present political and economic system, of which control over Ukraine's metallurgy is a fundamental part.

Arkadiusz Sarna

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¹ Ukraine showed the highest level of production (over 55 million tons of steel products) in 1988. In 1990, the USSR's per capita consumption of steel products (404 kg) was higher than the world average (127 kg) and the US figure (347 kg), Japan being the only country that showed higher consumption (752 kg). Ukraine accounted for the largest portion of the USSR's consumption. In 1993, the general figures for the CIS were two times lower (199 kg) than the lowest levels in 1998 (101 kg). V. Romenets, O. Yuzov, T. Rubinshtein, 'Metallurgia i rynek metallov stran SNG v 1990–2000 godakh' in *Metallsnabzhenie isbyt*, issue No 5, 2001. Today, Ukraine produces about 43 per cent of the CIS's cast iron, 36 per cent of its steel, and 35 per cent of its rolled products. Stepan Riaboshan: 'Proizvodstvo chernykh metallov v Ukraine', PROMETALL, 19 January 2001, (<http://www.prometal.com.ua/analit.php3?n=32>).

² See also: V. Pikovski, 'Problemy i prognozy razvitiya chernoi metallurgii Ukrainy' in *Metallsnabzhenie isbyt*, issue No 5, 2001, p. 34. With the region's most modern, though small, steelworks, Belarus and Moldova are performing best in the new reality. Over the last decade, these two countries have managed to regain and even considerably exceed the production levels of 1990. Meanwhile, the establishments in Azerbaijan and Georgia have become almost completely inactive. Romenets et al., *op. cit.*. The authors grouped the CIS countries as follows: 1) Belarus and Moldova, 2) Russia, Ukraine, Kazakhstan and Uzbekistan, and 3) Azerbaijan and Georgia. According to the authors, in 2000 as compared to 1990, the production of steel in particular groups changed as follows: group 1 showed 27.8 per cent increase; group 2 a 36.2 per cent decrease; group 3 a 96.8 per cent decrease.

³ International Iron and Steel Institute (http://www.worldsteel.org/trends_indicators/figures_3.html).

⁴ According to the Moscow State Institute of Steel and Alloys, Ukrainian exports of finished rolled products increased by 15 per cent in the 1990s, while sales to the CIS countries dropped seventeen times. At the same time sales to other countries increased seven times. Romenets et al., *op. cit.*

⁵ IISI – (http://www.worldsteel.org/trends_indicators/figures_11.html).

⁶ V. Pikovski, *op. cit.*

⁷ Data for 2000, based on: Derzhavnyi Komitet Statystyky Ukrainy, *Ukraina v tsyfrakh v 2000 roci*, p. 68, tab. 4.19 and 4.20, p. 69, tab. 4.22, p. 70, tab. 4.25.

⁸ The steelworks of Kriviy Rih (29th position, 6.1 million tons of production), Mariupol (Illich MMK, 33rd with 5.5 million tons), Azovstal (47th, 4.3 million tons), Zaporizhia (53rd, 3.9 million tons) and Alchevsk (70th, 2.9 million tons). For comparison, the IISI ranking also included six Russian steelworks and just one Polish plant (Huta Katowice). The volume of the 'great five's' turnover is comparable to the total turnover of Poland's ferrous metallurgy (http://www.worldsteel.org/trends_prod/prod02).

⁹ Cited after PROMETALL (www.prometal.com.ua/rating.php3 and <http://www.prometal.com.ua/rating.php3?quest=4>).

¹⁰ For comparison: overseas sales of the products of the chemical industry, i.e. the second largest exporter sector, amounted to over US\$1.5 billion (with a 10.6 per cent share in total exports), the sale of machines and equipment reached nearly US\$1.4 billion (9.3 per cent), and the respective figures for the flagship sector of Ukraine's economy, i.e. agriculture (including the food production

industry) were US\$1.4 billion and 9.5 per cent) – see: Derzhavnyi Komitet Statystyky Ukrainy, *Ukraina v tsyfrakh v 2000 roci*, p. 148, tab. 9.3 and p. 152, tab. 9.5.

¹¹ In the present paper, this term is treated as basic, although these specific organisations are also called 'corporations', 'holdings', 'concerns', and are sometimes in a broader sense termed 'clans'.

¹² See: 'Hromada – nowy faworyt ukraïnskikh vyborov parlamentarnykh' in *Tydzien na Vschodzie*, CIS, issue No 67, November 21, 1997.

¹³ Aleksandr Menshakov, 'Evropeiskaya Kolumbia' in *Kievskiy Vedomosti*, October 9, 2001. Gosplan – former State Planning Committee (abbreviation from Russian: Gosudarstvenny planoviy komitet).

¹⁴ Ibid.

¹⁵ *Ukraina v tsyfrakh...* – p. 65, tab. 4.12, p. 70, tab. 4.25 and p. 69, tab. 4.22.

¹⁶ After more than two years, Zviahlytskyi was 'amnestied' and returned to Ukraine to become the head of the management board of the Zasiad'ko mine in Donets'k (of which he had been a director in the early 1990s).

¹⁷ Donbass – shortcut for Donetskyi Basseyn (Donets'k Coal Basin).

¹⁸ See: Gwendolyn Sasse, 'Fuelling Nation-State Building: Ukraine's Energy Dependence on Russia', The Royal Institute of International Affairs, Russia and Eurasia Programme, Briefing Papers, April 1998.

¹⁹ This refers to the local clan's then leaders, Yevhen Scherban' and Akhat Bragin, among others.

²⁰ At that time, Lazarenko became the leader of Hromada, a party firmly opposed to the ruling group. In 1998, he was detained in Switzerland on a charge of money laundering. Released on bail, he spent a short time in Ukraine and left for the US, where he requested political asylum. He was, however, detained and accused of money laundering. The Ukrainian Prosecution Office accuses Lazarenko of having ordered the murder of Yevhen Scherban' in 1996, among other charges.

²¹ Formally, Akhmetov is the honorary president of the Shakhter Donetsk sports club (which he in fact owns), a shareholder and chairman of the board of directors of Dongorbank, the group's key bank, and a shareholder of an mysterious local company named Luks.

²² 'Donetske metallisty' in *Kompanion*, 26 September 2000.

²³ 'Usynovlenie KhTZ' in *Delovoy Donbass*, issue No 27–28 of 2001. Azovstal, IUD-controlled steelworks, supplied the Khartsyz'k factory with strips necessary for the production of steel pipes. This was done on an atoll basis: the factory in Khartsyz'k gave its finished products back to IUD, which then sold pipes on its own account. 'Trubnyi gigant menyayet khoziaina' in *Donetskie Novosti*, 30 August–5 September 2001.

²⁴ The state-owned gas monopoly which administers the westward transit of Russian gas.

²⁵ Derzhavnyi Komitet Statystyky Ukrainy, *Ukraina v tsyfrakh v 2000 roci*, p. 22, tab. 1.6.

²⁶ Based on *Ukrainskaya Investitsionnaya Gazeta*, quoted after PROMETALL (www.prometal.com.ua/rating.php3 and <http://www.prometal.com.ua/rating.php3?quest=4>). Data for 2000.

²⁷ Under pressure from the privatised energy distribution enterprises. The requirement imposed by the European Bank for Reconstruction and

Development to bring the energy prices to realistic levels became one of the main causes for the recent dispute between Kiev and the Bank regarding the terms for financing the Rivne and Khmelnytsky nuclear reactors construction – see ‘Ukraine–EBOR–Rosja: wokół projektu budowy reaktorów wChmielnickim i Równem’ in *Tydzien na Wschodzie*, CIS, issue No 250, 13 December 2001.

²⁸ *Polityka i kultura*, 4–10 December 2001.

²⁹ Formerly, Russian Yuzhmash.

³⁰ Kost Bondarenko, *Atlantydy i kariatydy*. L'viv, 2000, p. 96.

³¹ K. Bondarenko, *op.cit.*, p. 99.

³² Pavlo Lazarenko remains in detention in the United States, and Yulia Tymoshenko has returned to the ranks of the firm anti-presidential opposition following a short but important period (2000) of work in Viktor Yushchenko's government and her subsequent resignation.

³³ See: ‘YUGOK: ispravlenye oshybok’ in *Zerkalo Nedeli*, issue No 44, 2001 and ‘YUGOK pochty ne viden’ in *Zerkalo Nedeli*, issue No 43, 2001.

³⁴ According to the tax police, in the course of the investigation into the bank it was found that from 1996 to 2000 it had profited from financing the Zaporizhstal and Dniprospectal steelworks, the pipe factory in Nikopol and a number of ore enrichment plants (such as the Pivdennyi HZK). In the opinion of the tax police, the managers of these establishments had signed a contract under which products were supplied at reduced prices to companies registered in tax havens. As a result of this kind of co-operation with the bank, the enterprises' losses reached 1 billion hryvnas (about US\$200m). *Den*, 10 November 2001.

³⁵ Pinchuk is ‘accused’ of providing a number of other services to his father-in-law. In summer 2001, Mykola Tomenko, a well known political scientist and opponent of the president, maintained that the Agency for Humanitarian Technology (which Pinchuk owns) concluded a US\$500,000 contract with the Black, Kelly, Scruggs & Healey (BKSH) PR company of Washington for actions aimed at enhancing the image of Leonid Kuchma in the US. *Ukrainska Pravda*, 26 July 2001 (<http://www.pravda.com.ua/?10726-3-1>). Acting on the orders of the Trudova Ukraina party, the US detective company Kroll Associates carried out an investigation to clarify the case of the so-called Melnychenko tapes (the President's alleged role in the murder of Georgi Gongadze, an opposition journalist). On 25 September 2001 Kroll Associates challenged the reliability of these recordings. *Tydzien na Wschodzie*, CIS, issue No 240, 27 September 2001.

³⁶ Including Greece, Spain, Germany, Switzerland, Turkey, Italy, Canada, the USA, China, Iraq, Iran, Indonesia and Thailand – ‘INTERPIPE. Investytsyi v kachestvo’ in *Metalosnabzhenie isbyt*, issue No. 5 of 2001.

³⁷ PROMETALL (<http://www.prometal.com.ua/rating.php3>, <http://www.prometal.com.ua/rating.php3?quest=2> and <http://www.prometal.com.ua/rating.php3?quest=4>).

³⁸ At this moment it is worth considering the episode that took place in the early 1990s when Yulia Tymoshenko was to establish a joint enterprise (Russian *Sodruzhestvo*) with Viktor Pinchuk, but after some time quit this arrangement to join Pavlo Lazarenko. See: (<http://www.for-ua.com/person/207/167.html>).

³⁹ Zaporizhia Ferroalloy Plants is one of Europe's largest ferroalloys manufacturers (among other products, it manufactures alloys of silicon and manganese). It

exports about 80 per cent of its products. Dneprospectal is Ukraine's only producer of extra-fine steel, from which parts for Soviet spacecraft were produced.

⁴⁰ PROMETALL. Lenta Novostei (<http://www.prometal.com.ua/news.php?id=18951>).

⁴¹ Vadym Hurov, ‘Nevidkladni zakhody zderzhavnoi polityky v chornii metalurhii Ukrainy’ in *Holos Ukrainy*, 20 February 2002.

⁴² ‘Eksperyment udalsia. Chto dalshe?’ in: ‘O perspektivakh otechestvennoi metallurgii – Programma razvitiya chorno-metallurgicheskogo kompleksa Ukrainy’ by Stepan Seliverstov, 28 September 2001, PROMETALL (<http://www.prometal.com.ua/analit.php3?n=74>).

⁴³ Since then, up to 75 per cent of profits derived from the reduced tax rates were to be spent on modernisation.

⁴⁴ Remetall of Spain established the J.V. Intersplav company in 1989 by transforming the aluminium alloys plants in Sverdlovsk (the Luhansk oblast). The company sold its products to world powers in the automotive industry, including Fiat, Mercedes, Volkswagen, Toyota and Nissan. In 1998, Intersplav was awarded the international quality certificate ISO 9002. Business Information Service for the Newly Independent States, Luhansk Regional Report (<http://www.bisnis.doc.gov/bisnis/country/000307Luhansk-ua.htm>). The Swiss companies Bearco and Glencore co-operated with the titanium and magnesium complex in Zaporizhia (which produced special-purpose materials, including ferrotitanium) and Ukrtsink of Konstantynivka respectively. Glencore was mentioned as one of the companies interested in the privatisation of the aluminium works in Zaporizhia.

⁴⁵ In 1998, Metalsrussia (incorporated in the Virgin Islands, but with its main office in Moscow) controlled up to 57 per cent of shares of the Donetsk steelworks, the major portion of whose products was supplied to Russian machine-building plants. As a result of ownership transfers, Metalsrussia became a member of the ISTIL Group, and the Istil-DMZ company was established on the basis of the Donetsk steelworks' assets. Following further transformations, three new companies were established based on the Donetsk steelworks, and the state's attempts to sell a 16-per cent block of the steelworks' shares failed.

⁴⁶ For example Zaporizhstal, the fourth largest steelworks complex in Ukraine, remains within Russian oligarch Boris Berezovsky's sphere of influence according to unconfirmed information. ‘Komu prinadlezhyt Ukraina’ in *Ukrainskaya Investitsionnaya Gazeta*, issue No 2–3 of 2001.

⁴⁷ In the case of Russia, this was 70 per cent. V. Pikovski, *op.cit.*, p. 34.

⁴⁸ ‘Donetckie metallisty’ in *Kompanion*, 26 September 2000. The steel mill in Kerch, Crimea, which is controlled by IUD, supplies products for railways in Iran. (http://www.oaokmk.com/start_r.htm).

⁴⁹ Pikovski, *op.cit.*, p. 36.

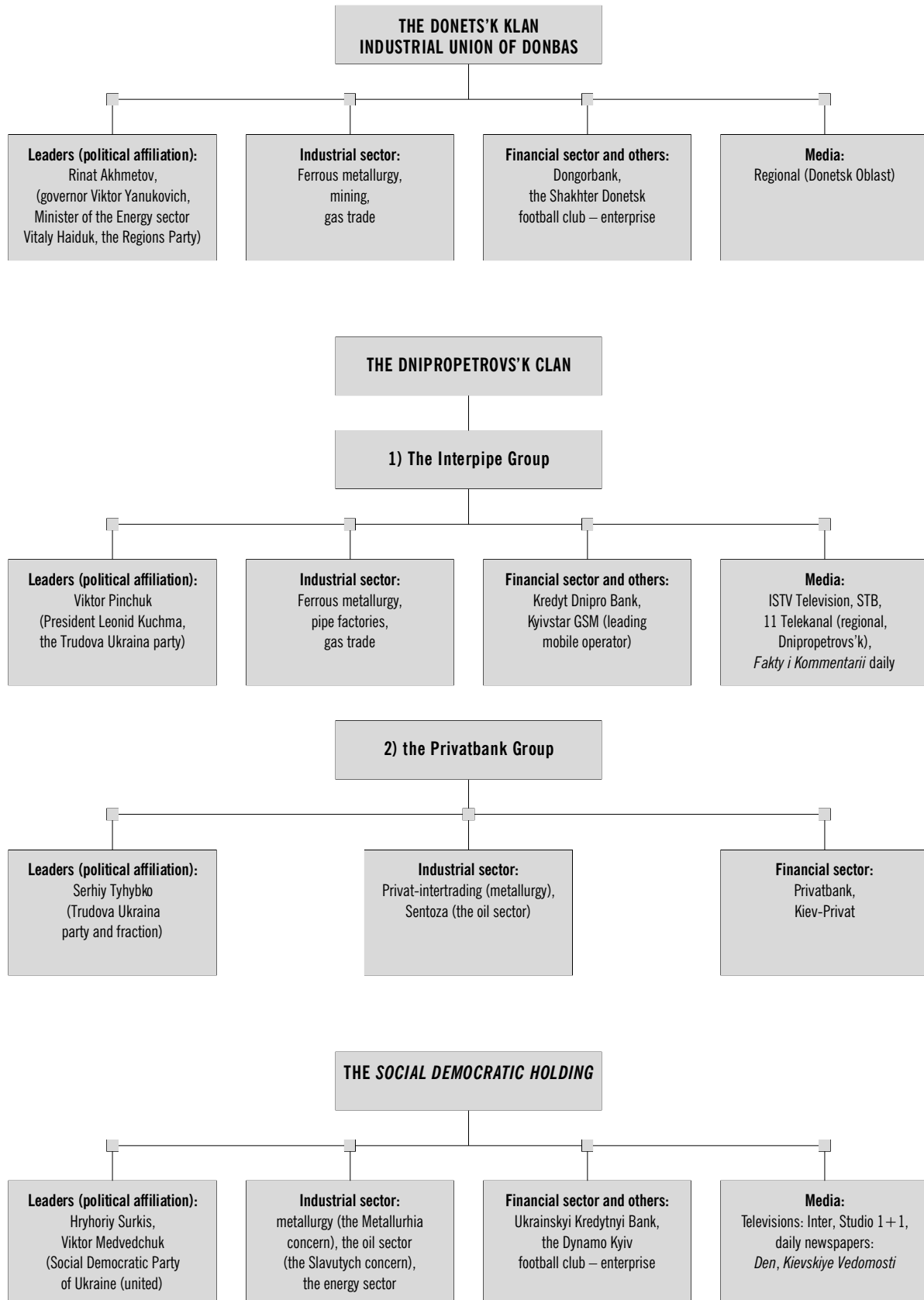
⁵⁰ IISI. (http://www.worldsteel.org/trends_prod/prod06 and http://www.worldsteel.org/trends_misc/misc07).

⁵¹ Pikovski, *op.cit.*

⁵² V. Hurov, *op.cit.*

⁵³ Ukrainian metallurgy consumes between 9 and 9.5 billion m³ of gas annually – ‘Metallurhy budut dobyvat haz?’, PROMETALL, 30 October–5 November 2001, (<http://www.prometal.com.ua/analit.php3?n=82&p=01>).

Appendix No 1: Main industrial and financial groups of Ukraine and their political backup



Appendix No 2: Basic figures of the Ukrainian metallurgy

Table 1. Selected items of Ukraine's industrial production in 1990–2000 (millions of tons)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Iron ore	105.0	85.5	75.7	65.5	51.5	50.7	47.5	53.4	51.1	47.8	55.9
Manganese ore	7.1	6.6	5.8	4.3	3.3	3.2	3.1	3.0	2.2	2.0	2.7
Steel	52.6	45.0	41.8	32.6	24.1	22.3	22.3	25.6	24.4	27.4	31.8
Rolled products	38.6	32.8	29.6	24.2	16.9	16.6	17.0	19.5	17.8	19.3	22.5
Steel pipes	6.5	5.6	5.1	3.1	1.7	1.6	2.0	1.8	1.5	1.2	1.2
Coke	34,7	28.4	27.3	20.4	16.9	15.8	15.1	16.4	16.4	17.3	19.4

Source: Derzhavnyi Komitet Statystyky Ukrainy

Table 2. Metallurgy as compared to other sectors of Ukraine's economy.
Industrial production dynamics in selected sectors in 1990–2000

Industry:	Percentage change over previous year										2000 to:	
	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	1990	1994
Electric power industry	-4	-6,4	-5,9	-12,5	-6,0	-6,9	-2,6	-0,2	6,6	-2,9	-34,7	-12
Fuels industry	-11,2	-14,5	-22,5	-17,2	-9,6	-6,7	6,2	-0,2	-0,8	-4,1	-58,6	-15
Ferrous metallurgy	-11,7	-9,7	-23,8	-28,8	-4,6	11,9	8,1	-6,8	6,2	20,7	-40,5	38
Non-ferrous metallurgy	-10,1	-16,3	-12,2	-26,3	-3,5	8	9,4	13,1	13,7	18,8	-14,3	74,2
Chemical industry	-7,2	-12,5	-25,2	-27,7	-9,3	-4,6	-1,4	1,6	0,3	5	-59,9	-8,6
Machine and equipment building industry	4,2	-3,6	6,1	-38,3	-23,9	-26,1	-0,2	-3	-2,1	16,8	-59,1	-37,7
Wood and papermaking industry	2,3	1,3	-2,8	-32,8	-17,4	-18,6	-0,9	7,9	21,5	37,1	-18,8	19,8
Construction materials industry	1,5	-3,7	-15	-37	-28	-34,2	-10,4	5,2	-1,9	-0,4	-77,1	-56,3
Light industry	-2,6	5,4	-13,3	-46,8	-32,6	-24,6	1,1	4,5	8,1	39	-61,6	-19,4
Food industry	-12,8	-14,5	-12,3	-18,4	-12,6	-7,2	-10,3	-1,1	7	26,1	-48,2	-3
Total industry	-4,8	-6,4	-8,0	-27,3	-12	-5,1	-0,3	-1	4	12,9	-43,3	-3,2

Source: Derzhavnyi Komitet Statystyky Ukrainy

Table 3. Geographic structure of Ukrainian ferrous metallurgy's exports

	1998		1999	
	(millions of tons)	(per cent of exports)	(millions of tons)	(per cent of exports)
Asia & Pacific	6	28.5	9.3	35.4
Africa, Middle East, Latin America	7.7	36.6	8.7	33.3
Eastern Europe	1.4	6.6	2.5	9.4
Western Europe	2	9.5	2	7.8
North America	1.6	7.6	1.9	7.1
CIS	2.2	10.4	1.7	6.5
Lithuania, Latvia, Estonia	0.2	0.9	0.2	0.5
Total	21.1	100	26.3	100

Source: V. Romenets, O. Yuzov, T. Rubinshtein, "Metallurhii i rynek metallov stran SNG v 1990–2000 godakh" in *Metallsnabzhenie i sbyt*, issue No 5, 2001.

Table 4. The sectors' shares in the value of sold production of the Ukrainian industry (per cent)

Industry:	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Electric power industry	3.2	3.5	6.4	9.4	11.5	11.0	12.6	12.6	16.5	16.2	12.2
Fuels industry	5.7	3.8	14.3	8.5	11.2	13.2	12.1	11.1	11.6	11.2	10.1
Ferrous metallurgy	11.0	9.9	22.2	16.8	19.9	21.8	21.6	22.7	22.9	23.8	27.4
Non-ferrous metallurgy	1.1	1.0	1.4	1.5	1.3	1.6	1.4	1.5	1.6	2.2	2.5
Chemical industry	5.5	5.4	6.4	5.5	6.4	7.0	6.7	5.9	5.7	5.4	5.8
Machine and equipment building industry	30.5	26.3	18.5	19.8	16.9	16.0	14.9	15.8	15.1	14.1	13.2
Wood and papermaking industry	2.9	2.9	2.2	2.6	2.4	2.2	2.2	2.0	2.2	2.2	2.3
Construction materials industry	3.4	3.7	3.6	4.7	4.0	3.9	3.3	3.3	3.3	3.1	2.6
Light industry	10.8	12.3	6.7	6.1	4.4	2.8	2.1	1.8	1.5	1.6	1.6
Food industry	18.6	24.4	13.6	19.7	17.1	15.1	16.3	16.9	14.9	15.1	17.4
Others	7.3	6.8	4.7	5.4	4.9	5.4	6.8	6.4	5.2	5.1	4.9

Source: Derzhavnyi Komitet Statystyky Ukrainy