

Survey
Impact of the
economic crisis on
Ukrainian companies



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Preface

Dear Readers,

We are pleased to present the results of the second Impact of the economic crisis on Ukrainian companies survey. Ernst & Young, a global leader in accounting and advisory services, conducted the survey from 30 January to 13 February 2009. Overall, 107 major Ukrainian and foreign companies working in Ukraine filled out questionnaires providing us with an update on their state of affairs.

Many participants of the survey are members of the European Business Association. We are grateful to the EBA for their kind support in running the survey and presenting the results to the public.

The first survey, conducted in October 2008, showed that almost 80% of the polled companies confirmed that their business has felt the impact of the downturn. The objective of the second survey was to learn how the economic crisis impacted the financial results and operational activities of companies, and what measures they are undertaking now to reduce costs. We were also interested to learn what programs would be considered a priority in 2009, how companies are planning their budgets, and what results they expect to achieve this year.

We believe that the results of the survey will be interesting to the Ukrainian business community. The survey gives market players an overview of the situation and will demonstrate how companies are meeting the challenge. We hope the results will contribute to raising overall awareness of the situation as Ukraine navigates these turbulent economic times.

Sincerely,

Ernst & Young

Impact of the economic crisis on Ukrainian companies

Introduction

We present the results of the second Impact of the Economic Crisis on Ukrainian Companies survey. The first was carried out in late October 2008, when Ukrainian companies first felt the effects of the crisis. This time the goal was to perform an update and study how the crisis impact on businesses in Ukraine has evolved, the top issues that companies are facing, how they are reacting to the changing economic conditions and how they plan to manage through 2009.

While the Ukrainian economy goes deeper into the economic downturn, most businesses are dealing with the effects of the crisis. In this sense, the development of the crisis in Ukraine follows global patterns; however, there are a number of trends specific to the Ukrainian context.

Ukraine enjoyed exceeding large business expansion in previous years, and most businesses formed their long-term plans and investment decisions based on the expectation that this trend would continue. Further roots of the current local challenges can be found in the unbalanced financial system, export-oriented natural resource industries, import-oriented market of finished goods and political instability.

Influence on Ukrainian companies

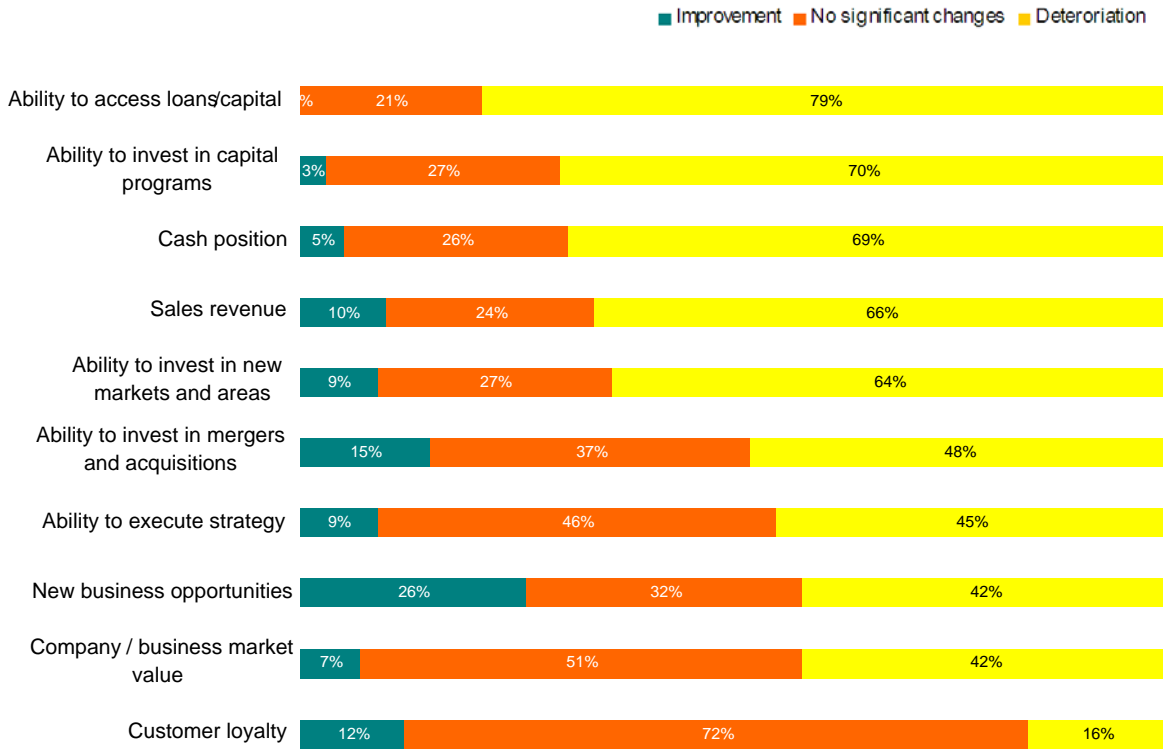
While the influence of the global economic downturn on Ukraine is certainly intensified by earlier plans and investment into never-ending Ukrainian growth, there are also challenges specific to the local market taking precedence over global trends.

As a result, Ukrainian businesses are giving more attention to managing domestic issues - devaluation of the Ukrainian currency, turbulent exchange rates, delays in payments, political risks, limited access to loans – rather than some of the broader global issues.

For example, three months ago in a similar survey, companies named their top problem as reduction in sales and demand. Today they cite decreased access to loans and capital and devaluation of the Ukrainian Hryvnia. Here we witness Ukraine moving into the next phase of the economic crisis on the back of local finance and currency issues. Financing the business and cost reduction are at the top of the agenda.

Difficult access to financing is not the only symptom of the worsening situation. Companies' sales volumes continue to fall. 66% of respondents have experienced deterioration in this area since the beginning of the economic crisis. 58% of businesses are already seeing lower quarter to quarter sales volumes in Q4 2008 than in 2007. At the same time, 44% of the respondents experienced sales volume reductions after the onset of the economic crisis back in the first half of October 2008.

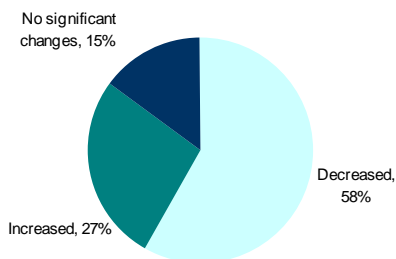
Impact of the crisis of companies' activities



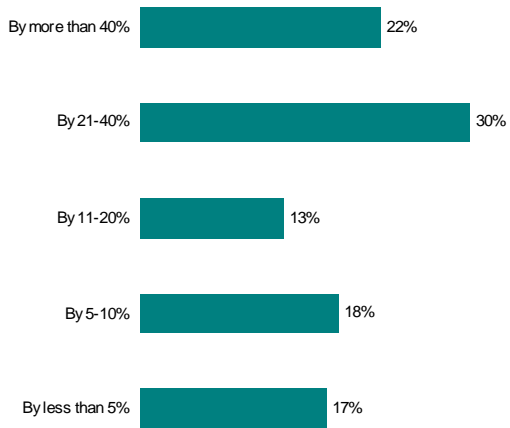
The amount by which sales volumes have fallen is even more important. Cumulatively, 65% of respondents reported more than a 10% decline in quarter to quarter sales volumes from the previous year, which is significantly more than the 25% who reported the same in the first half of October 2008. 30% reported declines as large as 21-40%, and 22% reported more than a 40% decline (Q4 2008 vs. Q4 2007).

49% of responding companies lowered production levels in order to meet the change in demand, while 16% increased and 35% did not change.

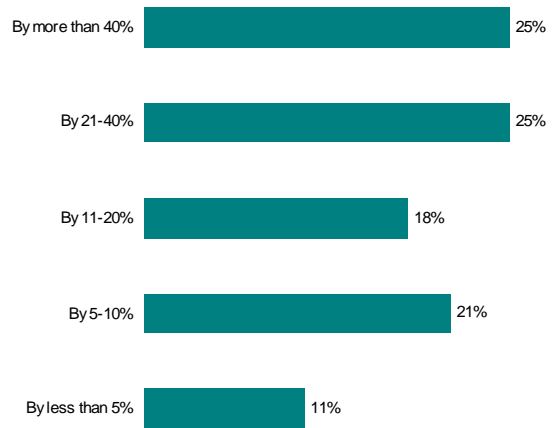
Changes of sales volumes in Q4 2008 comparing to Q4 2007



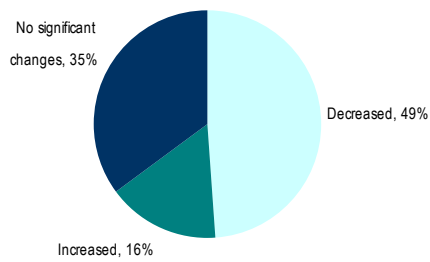
Decrease of sales volumes



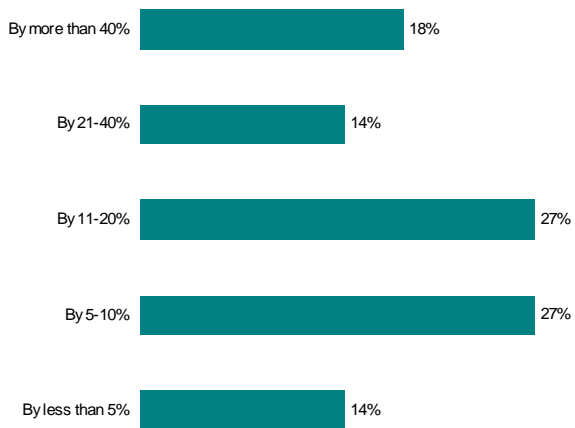
Increase of sales volumes



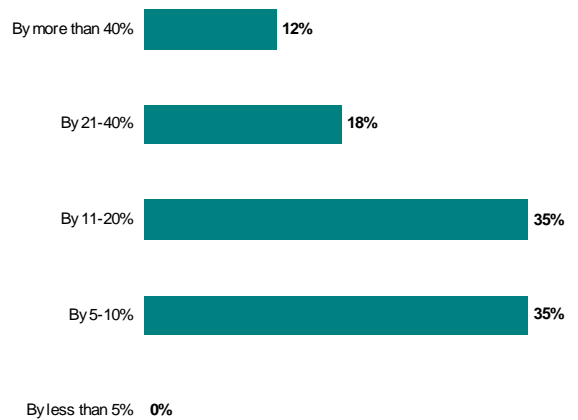
Changes in production/service capacity to meet the change of demand



Decrease in production/service capacity



Increase in production/service capacity



When asked what other business aspects are also showing signs of trouble, 79% of respondents noted decreased access to loans and capital, 70% indicated a weakened ability to invest in capital programs, while 69% observed a poorer cash position. All are financial in nature.

At the same time, respondents were reasonably more positive regarding non-financial aspects. 72% of respondents answered that they do not see changes in customer loyalty, while 12% even observe improvement.

46% of respondents see no changes in their ability to execute business strategy, and 9% of respondents believe they have even better chances now.

37% of respondents believe that their ability to invest in mergers and acquisitions has not changed, while 15% indicated their positions have improved.

32% of respondents see no changes in new business opportunities, and a solid 26% believe they have more opportunities now. These responses could be partially due to the less-tangible nature of these criteria.

Not all businesses are suffering in the current conditions: 10% of respondents see an increase in sales revenue and 5% enjoy a better cash position than before the economic crisis. Apart from the existence of specific niche markets, these results could also be explained by increased prices for products and services by businesses who tried to manage foreign exchange rate volatility and the connected risks.

27% managed to increase their sales revenue in the last quarter of 2008, compared to Q4 2007 results, while 15% maintained the same levels. This was made possible by rapid growth before the crisis.

Top issues that companies are facing now

We attempted to explain how changes in the economic environment have influenced various aspects of business in Ukraine. How do companies see the top issues they face now? Ukrainian businesses are concerned, above all, about the devaluation of the Ukrainian currency. The decrease in sales volumes ranked only fifth.

84% of respondents reported devaluation of the Hryvnia their top business issue. The substantial increase from the 46% who cited this concern in the October survey makes it the number one issue for Ukrainian businesses today.

66% are struggling with delayed payments by partners and clients, an increase from 53% in October.

54% are trying to reduce overall operating expenses while 53% are worried about the increased cost of financing.

51% reported concern for reduction in sales and demand for their products and services, compared to 56% in our previous survey.

Main problems that companies are facing at the moment

	% of companies
Devaluation of the hryvnia	84%
Delayed payments by our partners or clients	66%
Reducing our overall operating expenses	54%
Increased costs of financing or foreign currencies	53%
Reduction in our sales	51%
Concerns about inflation	47%
Decline of demand for our services	41%
Unavailability of capital	37%
Downsizing or laying employees	32%
Market fluctuations and, as the result, the reduced market capitalization of our company	15%
Other	5%
Company has not yet experienced the economic crisis	2%

Other issues

Defaults of banks
 Instability in banking system
 Postponing of Ukrainian projects
 Non-refunding of VAT

Companies' reaction to the downturn

77% of companies reported that they will treat cost reduction with much more importance given the foreseeable market conditions. It is no great surprise that cost reduction leads among planned responses to the change in the economic environment. This indicator has not changed significantly since October (76%).

Businesses opt for traditional ways of reducing their costs: 80% of respondents reported they are reducing or have already reduced administrative expenses, 57% are negotiating better terms with landlords or property owners, 51% are streamlining their operations, and 47% are going through reductions in personnel.

63% reported they will pay more attention to risk management. This could be explained by a large concern about the devaluation of the Hryvnia and delayed payments.

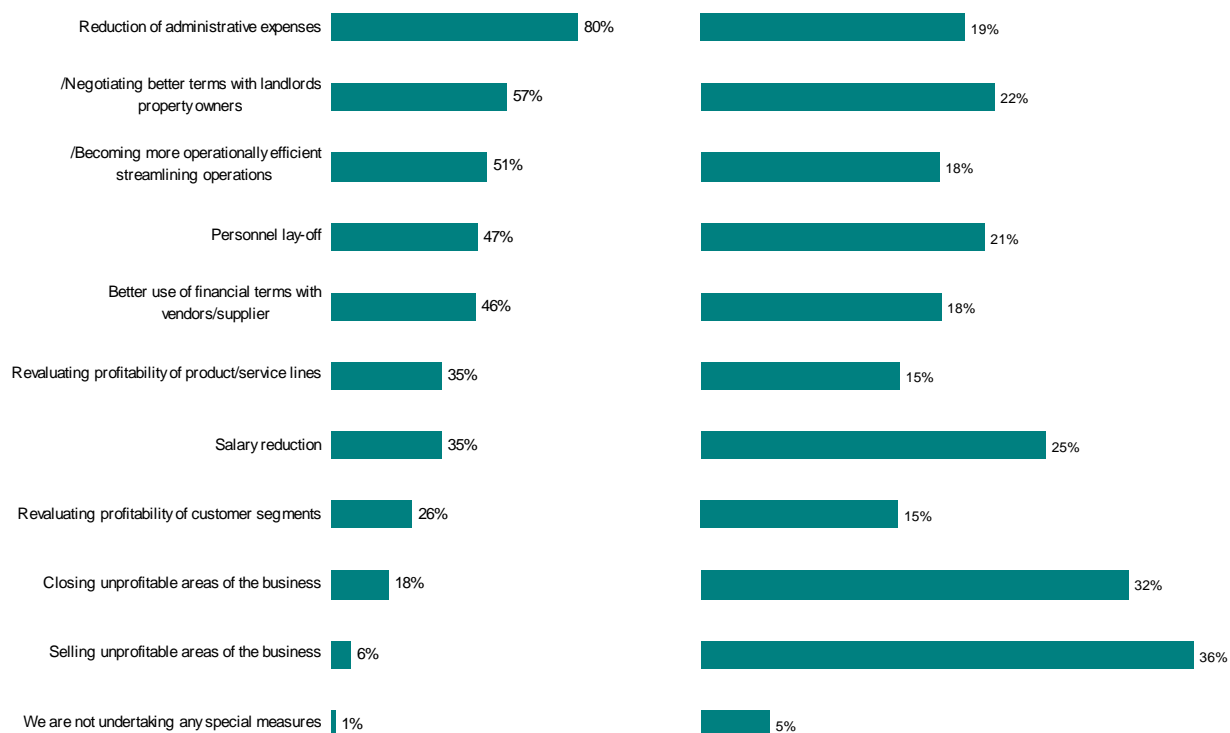
59% of respondents intend to focus more on customer relationship management as well as on working capital and cash management. No one indicated these responses in the previous survey.

Most companies have not yet reached the point of closing unprofitable areas of the business. Only 18% and 6% indicated that they are closing or selling parts of their businesses, respectively. These are the least popular options among cost reduction activities and, for the moment, businesses are looking at other options.

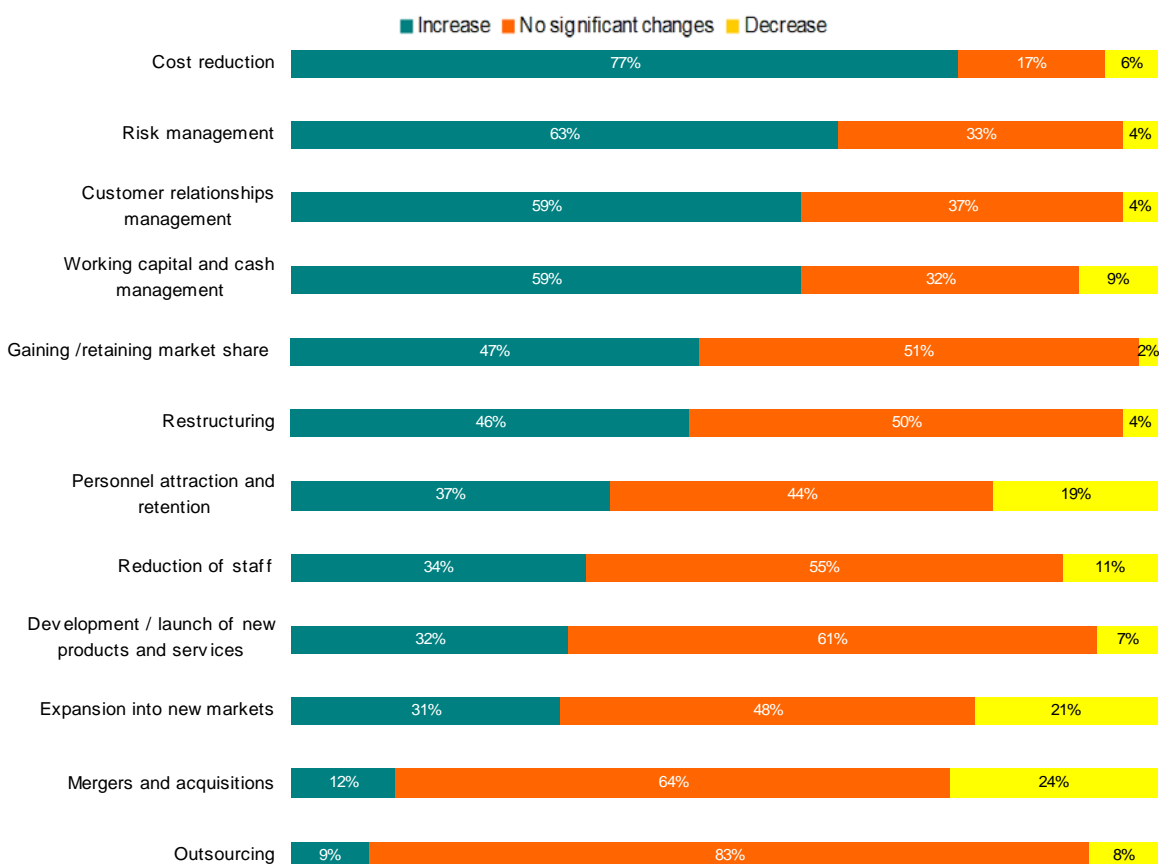
In addition, 83% of businesses plan no changes in their use of outsourcing. Given the consistent importance of cost reduction, this result is surprising and could mean that companies in Ukraine do not associate outsourcing with cost reduction.

Types of cost reduction activities undertaken

Estimated average percentage of reduction compared to pre-crisis level



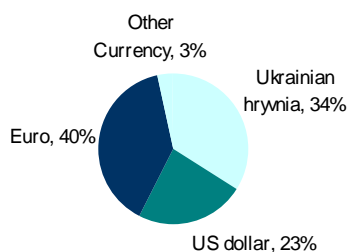
Activities/ programs that will change their importance to business



Planning in a turbulent environment

Most businesses in Ukraine use one of three currencies for planning and budgeting purposes: Ukrainian Hryvnia, US Dollar, or Euro.

Currency used for 2009 budget preparation

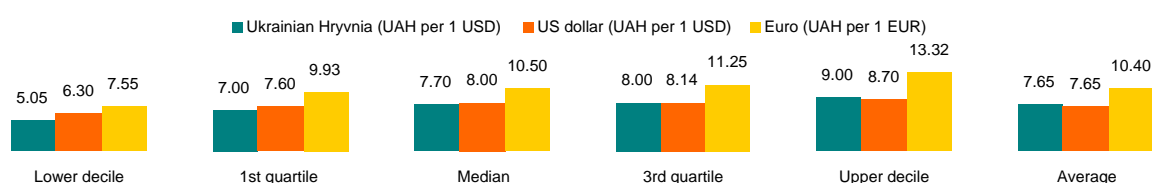


Two-thirds of respondents are planning their 2009 budget in a currency other than Hryvnia. The Euro is the most popular currency, with 40% of respondents reporting they are going to use it. For budgeting and planning, the range of exchange rate used was surprisingly wide - between 7.50 and 13.20, the average was 10.40.

34% of businesses use the Ukrainian Hryvnia as a major budgeting currency.

Finally, 23% of respondents use the US Dollar for budgeting purposes. The exchange rates used range from 5.05 to 9.00, according to most of the respondents.

Exchange rate used for 2009 budget, UAH per unit of currency



Other currency used for 2009 budget preparation

Danish Krone	10 UAH/GBP
NBU exchange rate	12.5 UAH/GBP

These results demonstrate companies' concern about the Hryvnia devaluation. Certainly businesses have to manage currency exchange risk throughout the course of 2009. The survey shows that, for this purpose, respondents are switching to using primarily a single currency in their business, daily currency buying/selling transactions, and linking business transactions to different currencies in order to obtain better diversification and reduce currency risk.

Of note, 36% of companies that switched to using primarily a single currency in their business use the Ukrainian Hryvnia for budgeting purposes.

33% of respondents indicated that they will perform more daily currency buying/selling transactions in order to manage exchange rate risk.

In addition, 25% of companies indicated they will diversify their risks by linking their transactions to different currencies.

Currency risk mitigation measures planned for 2009

	% of companies
Daily currency buy / sell transactions	33%
Transfer to primarily single currency	36%
Hedge transactions	15%
Diversification by linking transactions to different currencies	25%
Other	4%

Other currency risk mitigation measures planned for 2009

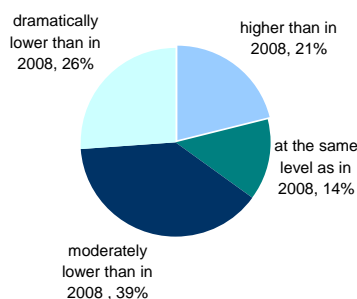
Agreement with clients on USD/Euro and immediate payments of invoices
Limit of UAH invoices validity time
Prices increase
Transactions in hard currencies only
Prices in UAH and quick prices adjustment

Local financing to allow hard currency transfer without exchange
20% more daily currency buying

Most respondents anticipate lower profits in 2009 than in 2008. Only one-third expect the same level or even higher profits than last year. 39% of respondents anticipate moderately lower profits, while 26% expect profits to fall dramatically.

Anticipated impact of crisis on 2009 profits compared to 2008

Profit is expected to be:



Over the three month period since the last survey, profit outlook has sharpened, either significantly improving or worsening. Comparing results with the outcome of the previous survey, 16% more companies than in October believe their profits will fall dramatically. Today, 21% of companies predict higher profits, while only 16% believed so back in October. 14% think their profits will grow at the same level compared to 34% of respondents in the previous survey. Since October, the total share of respondents expecting lower profits in 2009 increased by 15%.

Overall, the poll shows that the Ukrainian business community has become more pessimistic with regard to their business results in 2009.

Conclusion

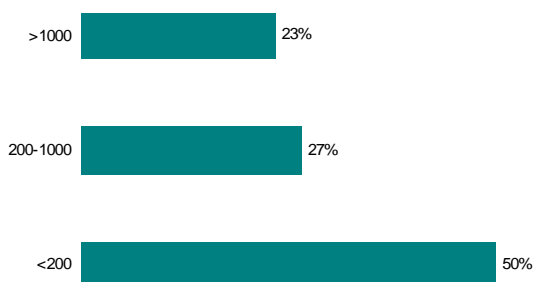
107 companies working in Ukraine and representing different industries took part in the survey. 18% of the companies are Ukrainian businesses; the other 82% are foreign companies that work in Ukraine. 50% of the participants represent small businesses (up to 200 employees), 27% are medium-size companies (200 to 1,000 employees), and 23% are big companies (over 1,000 employees).

The survey demonstrated that Ukrainian companies have become more concerned about risks in the Ukrainian financial system and more pessimistic regarding the financial aspects of their businesses. More optimism is indicated only in the non-financial aspects of their activities

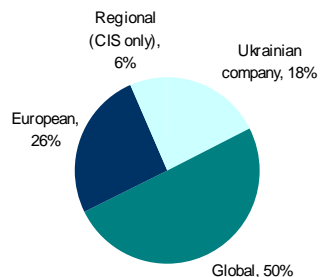
Most businesses have undertaken or are currently undertaking cost reduction activities and trying to manage risks connected with the Ukrainian financial system.

As the Ukrainian economy enters the next phase of the economic downturn and faces further challenges throughout the course of 2009, it will be interesting to see how these perceptions and their business realities change.

Total number of employees

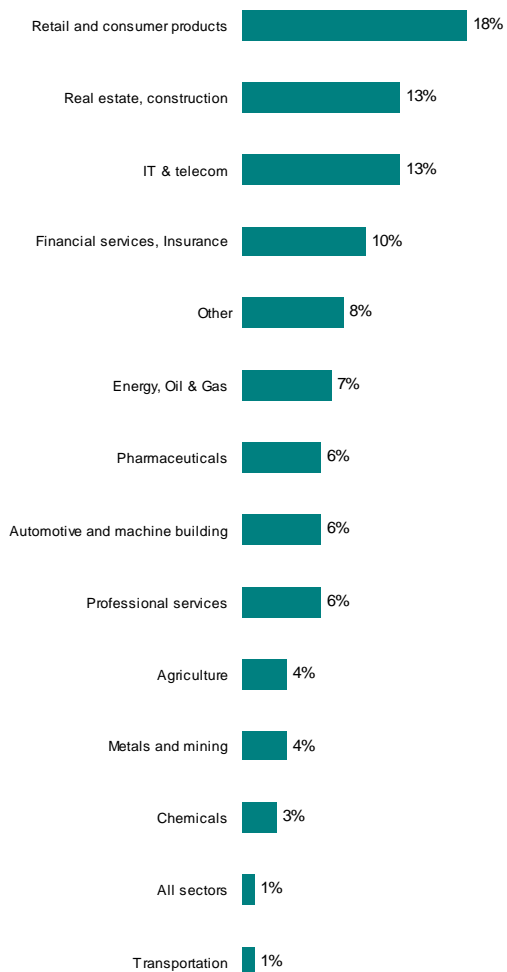


Region of company operations



Based on data of the companies that answered this question.

Industry



Global survey: Cash is king across the globe as corporates tighten their belts

Ernst & Young research into 350 global companies shows a challenging and rapidly changing business environment

On 16 February 2009 Ernst & Young presented a report “Opportunities in Adversity” that highlights how nearly 350 major global corporates are adapting their business strategies to a deep international recession and how their key priorities are evolving for the next 12 months.

The Economist Intelligence Unit on behalf of Ernst & Young surveyed in January 2009, 337 board members of international corporates, over half of which had turnover of \$10billion plus, on how the downturn had impacted on their strategic objectives and the way they do business.

As stress rises and the slowdown intensifies how are leading international companies responding?

Cutting costs internally and freeing up cash

The starting point for any business is cash and many corporates have already drastically tightened their belts. Nearly 40% of the companies surveyed felt that had been a significant deterioration in the business environment in their individual sectors with over a third noting competitors withdrawing and a rise in bankruptcies. More than two thirds have already implemented increased frequency of reporting risk to their boards.

The drive to cut costs has already impacted internal business strategy. Over 80% of respondents have already undertaken a major costs saving analysis, nearly two thirds had instigated a headcount reduction programme and over half had rationalised their IT spend. European companies were more likely than their US counterparts to look to cut costs on Real Estate and IT rather than cutting direct or indirect employee costs.

The credit crunch has forced companies to seek alternative ways of improving liquidity. Nearly half of all companies had disposed of or shut down parts of their business and 43% were looking at alternate short term finance facilities whilst 23% were considering options to renegotiate their debt covenants as well as proactively communicating with lenders, analysts and rating agencies and considering renegotiating debt covenants. Barely a quarter said the availability of cash was not an issue.

Hitting customers and suppliers equally hard

The companies surveyed have already been keeping a close eye on both their customers and their supply chain. And with good reason, as over half had seen a deterioration in creditworthiness of customers (nearly 60% in Europe) whilst over half said that some key customers are in distress, and that there was an increase in the time lag between customer order and cash collection.

Companies have adapted their strategies to fit with this new environment with nearly three quarters showing an increased focus on key accounts and over 40% developing new products. A third said that fears about existing customers meant they had broadened their customer basis and a third said they had terminated contracts with customers they perceived as high risk.

In terms of suppliers, respondents were split equally between two very different strategies. Half the companies surveyed have narrowed their supplier base to obtain more favourable prices or terms whilst the other half have broadened the supplier base to reduce the impact of the failure of a key supplier. The majority of companies are already communicating more proactively with suppliers, half were negotiating payment terms with suppliers more frequently and over a quarter of companies said key suppliers were experiencing financial distress.

Corporates batten down the hatches

Companies were also asked about their top strategic priorities over the next 12 months. The vast majority highlighted protecting assets, performance improvement and restructuring their business. In terms of cash management two thirds of those surveyed were considering top down review of current cash management and of cash flows, half building working capital measures into performance objectives of management and 36% considering possible assets that can be turned into cash.

And where will they be looking to save cash in the future?

There were some fairly consistent messages around where companies will continue to look for savings. Corporates said they expected significant or reasonable savings in their supply chain operations (58%), their sales and marketing (42%), Operations (56%) and IT functions (43%).

In strategic terms 40% of Global companies and 53% of European ones said they were actively considering selling non-core or non-performing business, an increased use of shared services centre (27%), increased use of outsourcing (31%), making strategic alliances (30%) and moving operations to lower cost locations (31%). Companies particularly saw an increased role for outsourcing for their IT, Logistics and Human Resources.

However a reasonable proportion of corporates saw the recession as an opportunity to expand with 34% globally and 38% in Europe thinking of making strategic acquisitions.

Emerging markets and growth

Whilst most developed markets were either perceived as stagnant or in decline companies still saw major opportunities in emerging markets. China (59%), India (45%), South East Asia (26%) and Eastern Europe (31%) were the areas of the world that most global companies believed would have the best growth opportunities. US companies tended to favour South East Asia over India whilst for European companies the reverse was true. Some 18% of companies expect significant growth still in emerging markets in the near future; the majority (57%) expect growth to continue but a slower pace than over the last two years and 25% growth to slow significantly.

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