



## DIRECTIONS OF OPTIMIZATION OF THE FINANCIAL FLOWS ALLOCATION INVOLVING FINANCIAL INTERMEDIARIES



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**A** The relevance of the article is due to the fact that unequal financial flows redistribution caused the need of determination ways of financial flows optimization. The aim of the article is substantiation of financial flows allocation in the economy of Ukraine through the regulation of the financial intermediaries' activities. The assessment of the dynamics of deposit and credit transactions of banks was given. A fact that the significant share of the bank financial resources are located in the financial sector has proven. This situation causes a shortage of financial resources in the non-financial corporations sector. Imbalance of financial resources redistribution between the sector of financial and non-financial corporations is one of the reasons for slow development of economy and the development of the crisis. It was found that in recent years the funds of the banks is reduced due to falling incomes and a loss of confidence to the banking sector. It is shown that non-banking financial intermediaries do not have a significant role in the financial flows allocation, since they place they financial portfolio in banks. Collective investment institutions are able to accumulate substantial financial resources, but they need a clear legislative regulation. Taking into account the identified problems in the financial resource allocations involving financial intermediaries directions of optimization of regulating their activities in Ukraine were developed.

**K** Financial intermediaries, financial flows, allocation, banks, non-banking financial institutions.

### НАПРЯМИ ОПТИМІЗАЦІЇ АЛОКАЦІЇ ФІНАНСОВИХ ПОТОКІВ ЗА УЧАСТЮ ФІНАНСОВИХ ПОСЕРЕДНИКІВ

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**A** Актуальність статті зумовлена тим, що нееквівалентний перерозподіл фінансових потоків між секторами економіки вимагає визначення напрямів оптимізації фінансових потоків. Мета статті полягає в обґрунтуванні напрямів оптимізації алокації фінансових потоків в економіці України через регулювання діяльності фінансових посередників. Дано оцінку динаміці депозитних і кредитних операцій банків. З'ясовано, що більша частина ресурсів банків залишається у фінансовому секторі, що зумовлює дефіцит фінансових ресурсів у секторі нефінансових корпорацій. Дисбаланси перерозподілу фінансових ресурсів між сектором фінансових і нефінансових корпорацій є однією з причин уповільнення розвитку економіки та розвитку криз. Виявлено, що протягом останніх років ресурсна база банків зменшується через падіння доходів населення та втрату довіри до банківського сектору. З'ясовано, що небанківські фінансові посередники не відіграють суттєвої ролі в алокації фінансових потоків, оскільки більшу частину інвестиційного портфеля вони розміщують у банках. Інститути спільного інвестування здатні акумулювати значні обсяги фінансових ресурсів, однак їх діяльність потребує чіткого законодавчого регулювання. На основі виявлених проблем в алокації фінансових ресурсів за участю фінансових посередників обґрунтовано напрями оптимізації регулювання їх діяльності в Україні.

**K** Фінансові посередники, фінансові потоки, алокація, банки, небанківські фінансові установи.

### НАПРАВЛЕНИЯ ОПТИМИЗАЦИИ АЛЛОКАЦИИ ФИНАНСОВЫХ ПОТОКОВ ПРИ УЧАСТИИ ФИНАНСОВЫХ ПОСРЕДНИКОВ

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**A** Актуальность статьи обусловлена тем, что неэквивалентное распределение финансовых потоков между секторами экономики требует определения направлений оптимизации финансовых потоков. Цель статьи состоит в обосновании направлений оптимизации алокации финансовых потоков в экономике Украины посредством регулирования деятельности финансовых посредников. Дана оценка депозитным и кредитным операциям банков. Определено, что большая часть ресурсов банков остается в финансовом секторе, что обуславливает дефицит финансовых ресурсов в секторе нефинансовых корпораций. Дисбалансы перераспределения финансовых ресурсов между сектором финансовых и нефинансовых корпораций являются одной из причин замедления развития экономики и развития кризисов. Виявлено, что на протяжении последних лет ресурсная база банков уменьшается вследствие падения доходов населения и потери доверия банковским сектором. Выяснено, что небанковские финансовые посредники не играют существенной роли в алокации финансовых потоков, поскольку большую часть инвестиционного портфеля они размещают в банках. Институты совместного инвестирования способны аккумулировать значительные объемы финансовых ресурсов, однако их деятельность требует четкого законодательного регулирования. На основании выявленных проблем в алокации финансовых ресурсов при участии финансовых посредников обоснованы направления оптимизации регулирования их деятельности в Украине.

**K** Финансовые посредники, финансовые потоки, аллокация, банки, небанковские финансовые учреждения.

**Introduction**

The economic dynamics of recent decades reflects the growing role of financial intermediaries in the financial flows allocation. Enhancing their activities has increased the gap between the financial corporations sector and non-financial sector and increase the risk of imbalances in financial markets. Unequal redistribution of financial flows between sectors requires identifying areas of optimization of financial flows. Optimization of financial flows should be aimed at the choice of financial resources attraction and allocation, which would give the opportunity to receive an equivalent benefit all participants of these relationships while maintaining market equilibrium. That is why there is a need to study the financial intermediary’s activity on the financial market of Ukraine and their impact on financial flows allocation.

The financial intermediary’s activities have long been the subject of economist’s attention. The impact of the financial companies on the development of the financial services market is presented in the works of D. Haydukovich [2]. B. Zymovets explores the role of financial intermediaries in the accumulation of financial resources for economic development. [4] V. Kovalenko and V. Korneev explore the features of the system of financial intermediaries and the specifics of their development in Ukraine. Western economists examine the regulatory role of financial intermediaries in the implementation of monetary policy (I. Anheloni and E. Faiya [10]), the role of financial intermediaries in the emergence of financial imbalances and crises (Ahariya B. and H. Naqvi [9] F. Smetts [11]). The current stage of development of

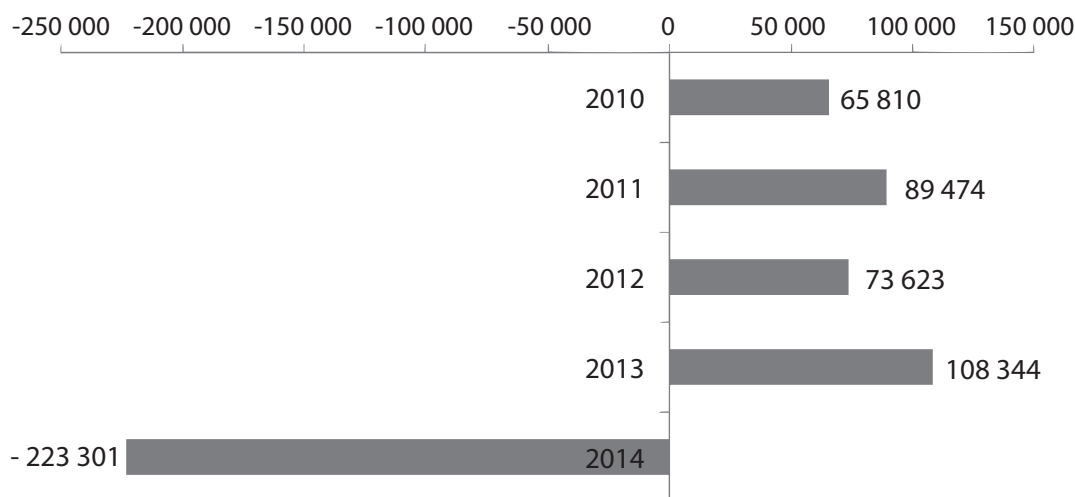
Ukraine’s economy requires new research about the role of financial intermediaries in financial flows allocation in unstable economies.

The purpose of the article – to prove the optimal methods of financial flows allocation in the Ukrainian economy through the regulation of financial intermediary’s activity.

Empirical and analytical studies. The financial intermediary’s activities are a constant search for donors and recipients of financial resources. The choice of raising funds form depends on the type of financial intermediary. Deposit institutions (banks and credit unions) attract financial resources through deposits. Non-deposit financial intermediaries attract funds under investment agreements (pension funds and insurance companies), providing specialized financial services (factoring, financial leasing). Mutual funds attract investment by issuing shares and investment certificates. Making decisions financial intermediaries primarily concerned to increase their own profits, often contrary to their role of institutional investors in the economy. Reconciliation the needs of the economy and the financial intermediaries, remains a key issue in the context of enhancing the role of financial intermediaries as institutional investors the economy.

In Ukraine, the most powerful financial intermediaries are banks. The worsening economic situation in Ukraine led to a decrease of bank deposits (fig. 1).

The positive dynamics during the 2010-2013 can be seen from the figure. This indicates that in this period more deposits were attracted by banks than have been returned. In 2014 the situation has reversed. A significant outflow of deposits in 2014 was caused by reducing the share of



**Fig. 1. Bank deposits in Ukraine in 2010-2014, mln UAH**

Source: calculated by authors [3].

individual’s deposits. One important reason for this is personal incomes falling and growing distrust in the banking sector. Distrust to bank system was caused by a bulk bank bankruptcy. For example, 19 banks went to bankruptcy in 2014, but in 2011-2013 only four banks had financial difficulties each year. Ukraine has a large number of small banks with high risky loan portfolios, very often they carry out currency speculation and involved in the conversion centers.

These banks undermine the reputation of the banking system and provoke decrease confidence in the reliability of investments into deposit accounts.

Ordinary consumers of banking services are not sufficiently protected in the case of banking institutions bankruptcy and the return of deposits to clients of bankrupt banks are imperfect. The procedure for the return of deposits stretched in time from 3 to 6 months. Particularly problematic are the return of foreign currency deposits. These deposits are returned in UAH equivalent at the NBU rate on the date of introduction of the interim administration. In terms of inflation and devaluation, investors lose a third of the cost of deposited money. This is not conducive to the restoration of confidence in the financial

sector. To increase the level of client's protection in the case of banks bankruptcy we recommend returning deposits in the currency of deposit account or at the NBU rate on the date of return.

Falling incomes also decreases deposits. Falling real wages index (fig. 2) means a reduction in the marginal propensity to save.

Index of real wages fell in 2014 to 86.5, which is 13.5 points lower than the standard value. Under such conditions most of the personal incomes used for consumption. So, not only banks suffer losses but also other financial intermediaries. The dynamics of deposits is crucial for banks' credit activity (fig. 3).

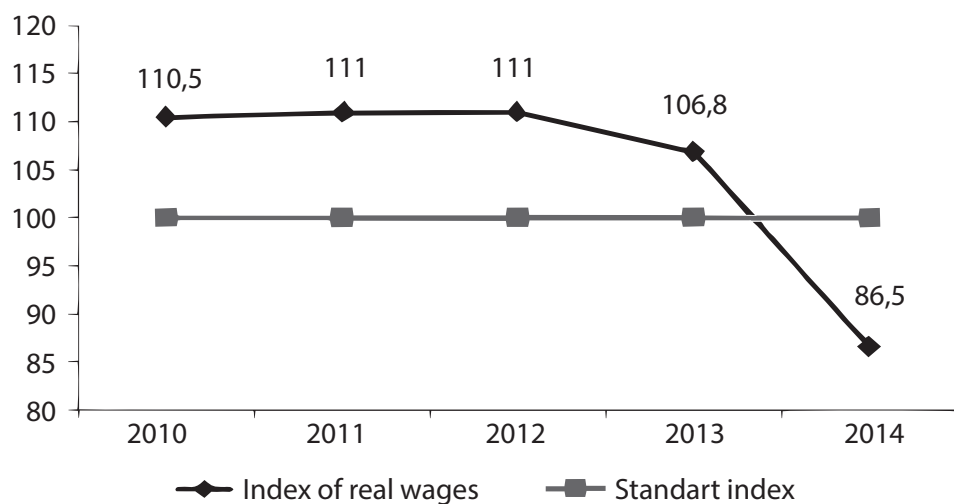


Fig. 2. Index of real wages in 2010-2014

Source: calculated by authors using data [6]

As shown in fig. 3, lending programs are curtailing, mainly because of the rising cost of credit. In 2014, the average lending rate for households was 27.11%, for enterprises – 17.64% (long-term loans). The lending reduction mostly affected sector non-financial corporations (fig. 4), which means economic slowdown in the medium term.

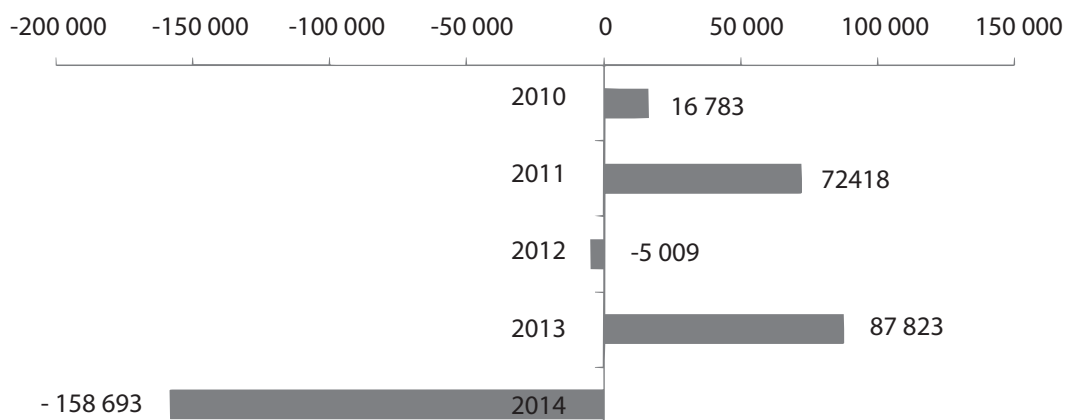
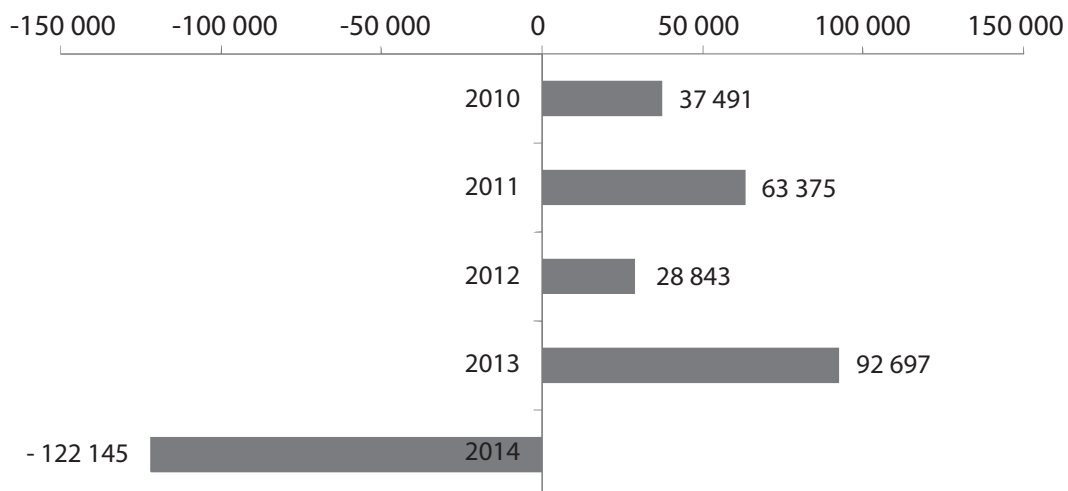


Fig. 3. Lending operations in 2010-2014, mln UAH

Source: calculated by authors using data [3]

The drop of lending operations was caused mainly by falling share transactions carried out by non-financial corporations. The low profitability of domestic enterprises does not allow them to attract sufficient amounts of loan because the cost of loan often can exceed the benefit which the company can get from using it.

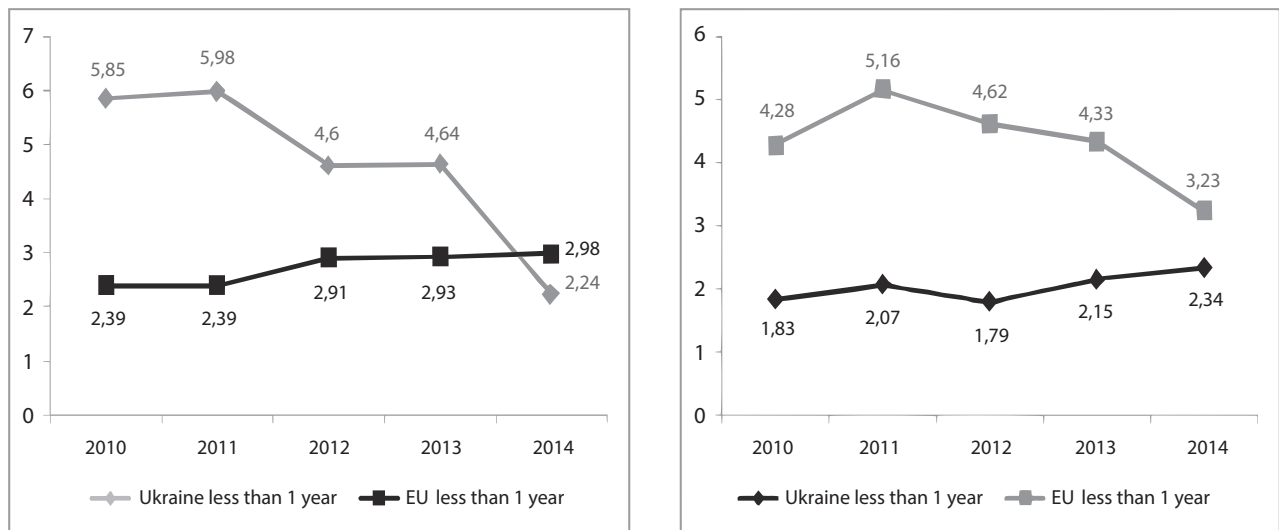


**Fig. 4. Loans to non-financial corporation in 2010-2014 pp., mln UAH**

Source: calculated by authors using data [3]

The level of interest rates is based on the NBU discount rate and the expected level of bank profitability. Taking into account that the discount rate and the spread remain very high, and lending rates cannot be lower. It should be noted that in Europe the level of spread is lower (fig. 5).

The banking sector in Ukraine typically have high level of spread, which means that banks are focused on high returns due to the formation of ultra-high rates on loans. Spread on short-term loans is higher. Indirectly, the profitability of non-financial corporations is influenced by spread as interest on loans included in the operating costs of



**Fig. 5. Spread the average weighted rates for of enterprises in Ukraine and the EU to 1 year and over 1 year in 2010-2014pp., %**

Source: calculated by authors using data [3]

businesses, reducing their operating profit. Therefore, the higher spread caused higher banks interest on loans and the lower profitability. This situation leads to allocation imbalances, manifested in the concentration of resources in the banking sector.

When the economy works on normal basis, this situation may not have negative consequences. But growth of bank lending spreads in a crisis will destroy the first non-financial corporations and then households. Potential instruments of regulation are to establish the maximum

rate and the upper limit of differentiation according to the average sector profitability. It is possible to apply the measures indirect impact on loan rates through the use of high income tax rate banks with high margin between lending and deposit transactions.

Non-bank financial intermediaries (private pension funds and insurance companies) usually put their reserves into deposit banks accounts. This is due to underdevelopment of the stock market and high yield deposit accounts (fig. 6-7).

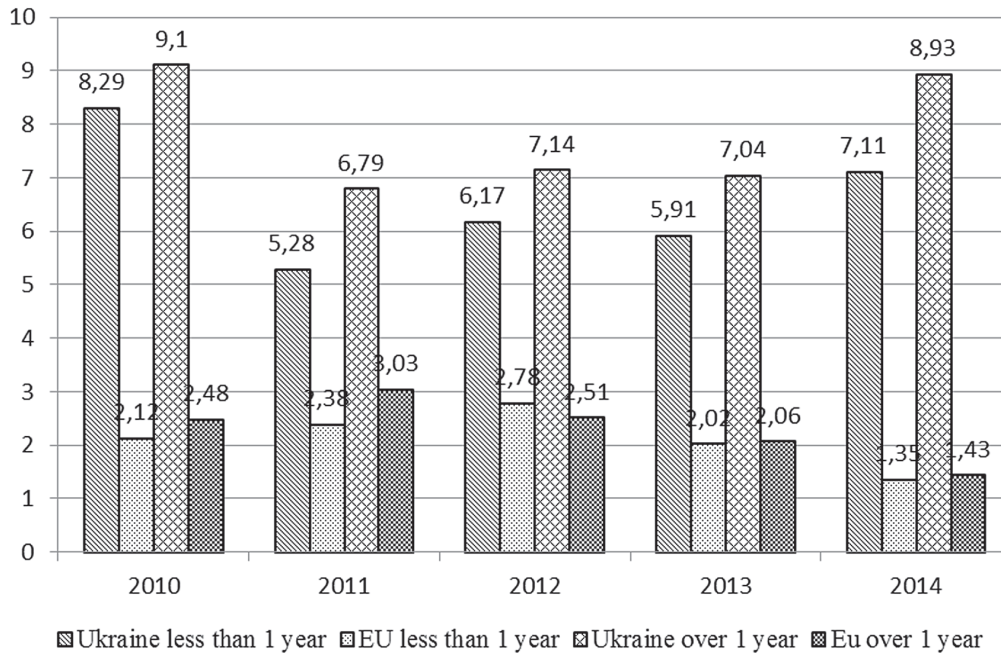


Fig. 6. Average rate on deposit accounts in EUR for households in 2010-2014 EU and Ukraine, %

Source: calculated by authors using data [1], [3]

Information in fig. 7 shows that the average rate on deposit accounts in the EU for businesses is lower than the rates on deposit accounts for households, indicating the orientation of banks to raise funds from the public. As a result, due to high interest rates on deposits financial resources continue to flow from one part of the financial sector to another, missing the sector of non-financial corporations.

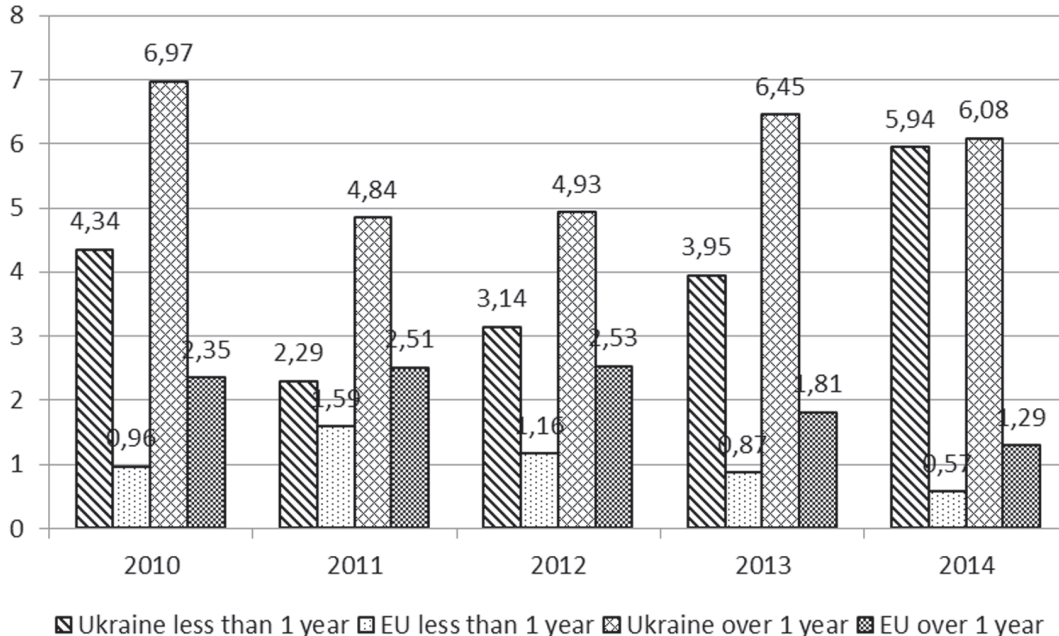


Fig. 7. Average rate on deposit accounts in EUR for enterprises in 2010-2014 EU and Ukraine, %

Source: calculated by authors using data [1], [2]

Non-bank financial intermediaries mainly used investment market in contrast to the banking. By volume of funds attracted the largest share of the market are mutual funds. The largest share of assets owned venture joint investment institutions (90%). With that in different from other mutual funds, this type of funds mainly invested in accounts receivable - 51.9%, «other investments» and shares the second and third places respectively [12]. The structure of venture mutual fund assets suggests that these institutions are often used for redistribution in the middle of the financial and industrial groups, tax evasion, and legalization of funds. Thus, an important area of optimizing the allocation of financial resources through joint investment institutions is to bring domestic venture capital funds with their classic

semantic content, which is funding high-risk innovative projects. It is necessary to apply a number of direct and indirect methods of regulation of institutional units, namely the legislation to bring the essence of venture mutual funds to the global experience, the use of fiscal mechanisms to counteract tax avoidance and more.

The powerful investors in the financial market could be pension funds and insurance companies that are engaged in long-term life insurance. These financial intermediaries accumulate long-term financial resources. The growth of the resource base depends on income and trust to this segment of the financial market. One of the options to increase public confidence is to create a deposit insurance system. Following the example of the banking sector it is possible to create a fund to guarantee insurance payments for life insurance contracts.

Another negative factor is the low level of income that is guaranteed by insurance companies (around 4%). The population is much easier to directly invest the same money into deposit accounts. In order for insurance companies to offer a higher yield, they should be able to diversify its investment portfolio. A promising area of portfolio diversification is the growth of the share of investments in mortgage-backed securities and direct participation in the construction, the latter option is more risky.

As known, an important investment rule «long money» is «long» nature of their investments”, and real estate is

stable and «long» tool for investment. According to the principle of comparability of time invested and received financial resources, convenient to invest in mortgage-backed securities / real estate maturity which does not exceed the term of concluded insurance company life insurance contracts. That is, the proportion of the portfolio of mortgage securities should increase in proportion to the share of long-term contracts concluded life insurance and meets them on time.

### Conclusions

The results of the study suggested the following areas financial flows allocation optimization in the economy of Ukraine through the regulation of financial intermediaries:

- guarantee the return of foreign currency deposits in the currency or deposit or in UAH at NBU rate on the day of return;
- the use of direct restrictions on the growth of the banking spread or indirect, through increased taxation of high profits banks;
- the development of life insurance segment and private pension funds. Perspective direction of expanding the resource base is the increasing quality of service, public trust by establishing Guarantee Fund insurance payments for life insurance contracts;
- regulation of collective investment institutions, directing their resources to non-financial corporations.

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