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## STRATEGIC PRIORITIES OF REGIONAL FINANCIAL POLICY MODERNIZATION

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**Abstract.** The author determines potential and real opportunities in the regions to ensure their socio-economic development based at sustainable usage of its own financial resources; critically analyzes existing mechanisms of financial management providing in the regions and identifies the causes of low efficiency. New directions to ensure effective financial management of the regions based on consideration of changes and opportunities created under the influence of intensification of integration processes in Ukraine and in the world economy are justified.

Finances of regions is regarded as part of local finances (according to the structure of the financial system of Ukraine) and are a system of economic relations on the creation, usage and distribution of financial resources between economic agents within a region in order to ensure its current functioning and development. Feature of authors methodological approach to the study of finance in the region is to give priority to the financial potential of the region formed over financial resources, allowing to expand the horizons of research by finances of the region, including their structure, along with the available financial resources of potential component, included along with budget potential financial capacity of the region, which is formed in the sectors of financial and non-financial corporations, and households.

**Keywords:** Regional Financial Policy; Local Budgets; Management; Regional Financial System.

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#### СТРАТЕГІЧНІ ПРІОРИТЕТИ МОДЕРНІЗАЦІЇ РЕГІОНАЛЬНОЇ ФІНАНСОВОЇ ПОЛІТИКИ

**Анотація.** Виявлено потенційні та реальні можливості соціально-економічного розвитку регіонів на базі раціонального використання власного фінансового ресурсу. Представлено критичний аналіз діючих нині механізмів реалізації регіональної фінансової політики й виявлено причини їх низької ефективності. Обґрунтовано нові напрями забезпечення ефективного управління фінансами регіонів на основі врахування змін і можливостей, що створюються під впливом активізації інтеграційних процесів в Україні та світовому економічному просторі. Визначено стратегічні пріоритети модернізації регіональної фінансової політики в контексті сучасних викликів національного і глобального середовища.

**Ключові слова:** регіональна фінансова політика; місцеві бюджети; управління; фінансова система регіону.

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#### СТРАТЕГИЧЕСКИЕ ПРИОРИТЕТЫ МОДЕРНИЗАЦИИ РЕГИОНАЛЬНОЙ ФИНАНСОВОЙ ПОЛИТИКИ

**Аннотация.** Определены потенциальные и реальные возможности регионов в обеспечении их социально-экономического развития на базе рационального использования собственного финансового ресурса. Представлен критический анализ действующих в настоящее время механизмов реализации региональной финансовой политики и выявлены причины их низкой эффективности. Обоснованы новые направления обеспечения эффективного управления финансами регионов на основе учета изменений и возможностей, создаваемых под влиянием активизации интеграционных процессов в Украине и мировом экономическом пространстве. Определены стратегические приоритеты модернизации региональной финансовой политики в контексте современных вызовов внутринациональной и глобальной среды.

**Ключевые слова:** региональная финансовая политика; местные бюджеты; управление; финансовая система региона.

### 1. Introduction

The dominant tendency of the national economy in the XX-XXI century is invigoration and increase in regionalization, which on the one hand raises the issue of weight transfer decision-making process of socio-economic system at the regional level, and on the other – imposes liability on regions for the effective financial policy aimed at developing a sufficient resource base to implement them. In such circumstances, it is extremely important to consider global and national factors of financial development in the region. International experience shows that the financial system does not perform regulatory functions to stimulate real economic activity, financing of investments in the real sector and provide a basis for economic growth and employment. As a result of the increasing polarization in terms of their socio-economic development, the struggle for seizure of financial markets, possession of raw-material and financial resources increases the risk for the territorial integrity

of independent countries. Thus, Russia's attempts to retain control over the Ukrainian government, financial and economic systems of Ukraine, to prevent the implementation of Ukraine's European aspirations, which led to the annexation of the Crimea by Russia and the military conflict deployment in eastern Ukraine, deteriorates socio-economic situation of the country.

The accumulated global macroeconomic and macro-financial imbalances require reform of the national financial system of Ukraine. However, we must admit that inefficiency of external security mechanisms of Ukraine's financial system is more significantly aggravated by internal problems, which are currently hindering development of financial relations in the country and reducing their effectiveness. Among them are permanent reform of Ukraine's economy and banking sector in particular, which often has the character of «pseudo» unstable socio-economic environment; irresponsibility of officials for decisions and their practical implementation; high level of corruption of all

branches of government; worsening of the social problems in the country. As a result, the reform of public administration and finance sector towards decentralization and delegation of authority to the local level and financial resources, which declared each new government for decades, have not been actually implemented. Moreover, in practice, takes place strengthening of administrative and financial resources centralization.

### 2. Brief Literature Review

Analytical review of publications has shown that the theoretical basis of the regional financial policy in developed countries is based on modern theories that provide empowerment of local authorities to use financial resources in developed regions; the socio-economic environment for the benefit of communities and preserving their characteristics in shaping the socio-cultural values; deepening of democracy and openness in financial relations formation between the state and the regions, while maintaining the balance in the financial policy.

We should take together key theories that form the basis of studies, necessary to distinguish two blocks. The first unit should include theories relating to building financial relations «state – regions» and allow forming approaches to financial management at the regional level: the theory of fiscal federalism (Musgrave, 1989 [1]; Chibu, 1956 [2]), the public choice theory (Brennan & Buchanan, 1980 [3]), the theory of decentralization (Prydomm, 1995 [4]; Tanzi, 1995 [5]). They are designed to ensure disclosure of regions' internal capacity by improving autonomy of regional and local authorities in the formation and usage of financial resources created by the entities located in their territory. The greatest recognition and practical use in European countries became: the theory of fiscal federalism and decentralization theory. Studies have also shown that these theories are not perfect, that is, with certain limitations on the effectiveness of their use. In particular, the theory of fiscal federalism requires a stable financial situation not only in the country, but also in the regions, the availability of financial reserve funds that can prevent crisis situations. The experience of European countries that are part of the EU in construction and usage of financial relations on theoretical principles of fiscal federalism shows that contradictions between the states exacerbate in a growing crisis, so regions need to regard directions and mechanisms of their financial resources forming.

The second block of theories are those that define the areas of the regions' financial potential implementation as a major factor in the formation of their competitive status in the national and global economic environment, in particular, the concept of «new regionalism» (Keating, 1998), the theory of the «center-periphery» (Friedmann, 1979), the theory of uneven spatial development (Amos, 1988), the concept of global regions (Chuzhykov, 1988).

### 3. Results

In Ukraine, studies have shown that the theoretical approaches to the formation of a regional financial policy are based on consideration of the achievements of the international community. However, by now no universally recognized definition of requirements for terminology related to the subject of research that not only complicates the process, but also can lead to erroneous results. Note that in the financial science using the concept of «finance of region» at the moment is not established, often domestic finance scholars identify the region of local finance or local government finance.

Thus, the financial component of the region is the Local Finance (according to the structure of the financial system of Ukraine), and it is a system of economic relations on the formation, usage and distribution of financial resources among economic actors within a region to achieve the current operation and development.

The system of the regional finance is regarded as the financial subsystem of the state (its operation is in accordance with the regulatory framework, principles and imperatives of targeted public finance) and, at the same time, as a set of structural elements that are defined according to the structure of the financial system in the region. Theoretical and practical feasibility of singling out research of finance in the region is reasoned by a range of internal and supranational factors.

Today, in terms of the implementation of local government reform and fiscal decentralization, government has made a number of steps to transfer resources and responsibilities to the local level – village, town, and city. Thus, there is a transfer of weight management process and, therefore, the concentration of financial resources of the region at the level of territorial communities and transform the region into a «statistical unit». This is in line with European trends reform of the administrative-territorial structure and principles of civil society, in particular the principle of subsidiary. Without denying the economic and social feasibility of implementing these processes, we consider it necessary to establish certain limits of their adequate Ukrainian practice. After all, blind imitation of the world experience without local realities can carry a number of risks and threats to Ukraine as a whole. Thus, excessive weakening of regional exposure and its financial base may stipulate:

(1) improving the socio-economic differentiation of regions for the GRP, local budgets revenues, income, etc. (these indicators Ukraine today is far above the European countries);

(2) increased concentration of economic expansion space and habitat depression, due to the concentration of financial resources in the centers of development and their «spillover» through the banking system with the less prosperous regions to more prosperous;

(3) improvement of intra differentiation. First and foremost, the strengthening of the gap between urban and rural areas, leading to an increase in the number of subsidized rural and rural local communities;

(4) disintegration of national economic space and ineffective functioning of the internal market, and, in turn, a direct threat to the integrity of the state.

Preventing and addressing threats outlined requires strengthening the role of territorial development instruments of financial regulation, implemented at regional level. The feature of copyright methodological approach to the study of finance in the region is laying in their foundation and giving priority to the financial potential of the region formed over financial resources. This allows expanding the horizons of finance research of the regions due, firstly, to the inclusion of their structure, along with the available financial resources of potential component; secondly, inclusion the households, along with budget potential financial capacity of the region, which is formed in the sectors of financial and non-financial corporations. In addition, this approach is the basis for the paradigm of management modernization at the meso-level – rejection of simple allocation of scarce budgetary resources of the region and transition to the implementation of effective methods of encouraging the rational (at market criteria) formation, usage and increase the financial potential of the region in all sectors.

The financial potential of the region determines the ability of the financial system in the region to ensure growth and development in the short and long term by maximizing the accumulation and efficient use of available financial resources and the conditions created by government, business and households in the region for achieving financial results, providing expanded reproduction and social development [6]. This criterion by the terms of the achievement of the goals are relying on their own sources of financing current needs of the region; ability of involvement in required quantities and at reasonable terms of external resources; formation of the resource base at an acceptable level of risk; presence of institutions providing financial management efficiency in the region.

Considering the peculiarities of reforming the national economy and the complexity of the situation in which the state finds itself as a result of the growth of contradictions in global, international scope, issues related to the assessment of their financial capacity to ensure the development of the country and its regions have become extremely important and need conducting major changes in methodology of state regional development policy formation based on consideration of resource, economic, social, environmental, territorial and geographical and other characteristics of each region. The main of them are:

(1) decentralization of the state budget during the formation of inter-budgetary relations must be determined by the ability of

regions to self-development. This necessitates the evaluation of the financial capacity of each particular region connecting them simultaneously with tactical and strategic objectives of socio-economic development;

(2) a legitimate raise the question of the need to assess financial capacity of self-development of each region that could form the basis for sound management decisions on the choice of areas of regional development, determining needs for transfers and attracting foreign investment have to be considered;

(3) as an integral part of spatial-territorial structure of the state, the regions of Ukraine are rather more complex system of financial accountability, than various financial institutions of the state, engaged in the distribution and redistribution of financial resources function. This requires installation on the legal basis of clear mandates of each distribution relationship participant with the general principle of social justice in resource potential using.

The integral indicator, based on which has to be formed the skeleton of financial relations between the state and the regions proposed to accept the value of financial potential of latter. The set of financial potentials of regions of the country forms the financial potential of the country. However, within certain regions, there are significant differences between the amounts of generated and used financial capacity. Most regions of Ukraine, as is known, ensure necessary financial resources for socio-economic development not only from its own resources, but also from subsidies from the state budget. Thus, the existing schemes of distribution and redistribution of the state budget between regions takes into account only their needs and ignores the possibility of accumulation of own financial resources, and the effectiveness of the management system of the region. Lack of interconnections between the needs of regions in financial resources and possibilities of their accumulation for the achieving of mentioned tasks is a key reason for subsidies of most domestic regions, and passivity of local authorities in the search for new sources of creation and effective usage.

Thus, based on the above mentioned, the financial imperative to ensure the development of regions of Ukraine in regional policy should become the individual (selective) approach to identifying the resource (including financial) potential of each region and evaluation of real possibilities of its usage for a specified period of time. The feasibility of using such approach is also confirmed by the following statements:

1. According to territorial principle, most of regions of Ukraine are larger than many European countries, but significantly differ from them by indicators of the degree of autonomy in the formation and selection of areas for socio-economic development. Increase of autonomy of domestic regions in the selection of areas of socio-economic development is based on the current legislation of Ukraine, but contradicts the principles of administrative and command distribution of powers between government institutions on the use of resources of regions, that within the decades are used in the state.

2. Each region of Ukraine is unique by its natural resources, geographical and climate conditions, and the composition of industrial and economic structures, their usage and pace of development. Features of the historical development of different regions of Ukraine determine the necessity of incorporation along with indicators of economic, social, spiritual and cultural values of the population that live there.

The essence of the selective management of regional development lies in selective impact on regional development, particularly in segments where market regulators are unfound. This policy is designed to resist the excessive growth of asymmetry of regional development in the social and economic spheres through the use of compensation (for areas with low levels of financial and economic capacity) or competitive (for areas with high levels of financial and economic capacity) mechanisms.

Features of the regional development in Ukraine demonstrate unreasonableness of rejection from the policy of compensatory nature and confrontation of its problems with competition policy of state regulation. Compensatory regional

policy is aimed at supporting of regions-recipients through intergovernmental transfers, and competitive measures on intensification of entrepreneurial activity and innovative processes in the regions, formation of competitive interregional economic systems in the national and global environment by targeting state investments and investment programs implementation. This approach allows reduction of inter-regional asymmetry by activation the mechanisms of spatial resonance distribution of development and reduction the gap between «growth points» and peripheral areas.

However, the transition to a selective type of state regional policy will require definitive typology of regions (for the reference to a particular group) with clearly defined criteria and indicators. Otherwise, individual approach to the selection of financial provision of regional development instruments could become another platform for certain regions lobbying and deepening corruption in the allocation of resources (such problem is inherent at present-day to the Regional Development Fund, which turned it from recognized by international practice progressive tool of support of regions in fund of financing lobbied regions). Regions of Ukraine have real opportunities to improve their financial capacity by improving the management of their own financial resources. However, their implementation requires substantially modified changes not only in the methodology of public policy for regional development, but also in managing their own financial potential.

As already mentioned, decentralization is one of imperatives of public finance development in Ukraine. However, despite the broad stream of publications about search of mechanisms for its implementation, its optimal scale still has not been determined. The question is: what proportion of funds should remain in place, and which needs the state for effective performance of its functions? The economic science proved a direct relationship between the level of intra-regional socio-economic differentiation in the country and the optimum level of centralization. That is, the higher the level of intra-regional economic differentiation, the greater the share of income should be centralized to ensure equitable distribution of income across the national economy. The centralization of fiscal authority is justified to a level that can increase the value of the public welfare function in all regions through income redistribution within the country.

Using the method of a probability modeling to assess the impact of fiscal decentralization based on the evaluation and comparison of the social utility of regional residents, we revealed the discrepancy in the current level of centralization of financial resources and powers conferred on regional authorities in Ukraine's economy. Even while maintaining the existing level of interregional differentiation in GRP per capita, local budget revenues and incomes of the population in different regions with the optimal level of centralization of budgetary resources in Ukraine should be within 36-40%. We can say that the level of resource withdrawal of regional budget to the state budget for 2006-2013 was twice from optimum value. Achievement of calculated level of centralization requires not just partial changes in the budget and tax policy of Ukraine, but systemic reforms and their restructuring on the new paradigm principles. Filling of local budgets cannot be made only from local taxes and property taxes; solution of this issue lays in the dimension of transfer to the local level a large part of national taxes. Under the present conditions, in Ukraine is hardly possible solution of problems of simultaneous increase of local budget revenues and reduction of major taxes.

While reduction of intra-regional economic differentiation opportunities to take advantage of decentralization become much wider. Taking into account this, state strategy of socio-economic development should include review of fiscal powers distribution between levels of government for the inter-regional economic differentiation reduction. In the conditions of active processes of globalization of the world economy, regional development cannot take place only under the influence of policy of national government or local communities. On formation of socio-economic status of Ukrainian regions have absolute effect such factors as their participation in global processes and international competitiveness of regions. It is the presence of capital



and its determination to overcome limits of the region which is the driving force and a prerequisite to attract the region to integration and competitive interactions in the global economic system. Furthermore, globalization expands the region and its economic entities to various financial instruments and the large amount of available capital, which should recognize the main advantage of financial globalization for Ukraine today.

However, international experience shows that not all regions that have a significant financial and economic potential are able to use the potential of globalization: few have become competitive in world space, and the rest have transformed to the global periphery. The reasons for this, we believe, lies in the dimension of their capacity and ability to take timely decisions about its development of competitive sectors of the economy, consolidation of efforts on the formation and development of internal market, realization of domestic producers support strategy.

#### 4. Conclusions

The carried out researches has proven the necessity of financial management imperatives formation the regions, which determine the directions of regional financial policy modernization:

1. Finance of region should play crucial role in building a convergent model of regional development, both on interregional and intraregional levels.

2. Transition from the simple allocation of budgetary resources, available to the region, implementation of financial mechanisms that provide incentives and active involvement of finance and people in the region, as well as foreign investors for the regional system development.

3. Denial of total approach to regional policy and its organization on the basis of individual, selective approach, in order to ensure the development of regions in terms of their financial and economic potential and a set of other objective factors.

4. Size of the region's financial potential should become an integral basic factor for the financial relations between the state and the regions forming. It will increase the local authorities' accountability for efficient formation, usage and accumulation of endogenous financial potential.

5. Practical implementation of fiscal decentralization in public finance to a reasonable level through the money transfer to the local level, along with local taxes and property taxes, will ensure the financial viability of individual regions and local communities, as well as start the processes of their development based on stimulating of their own financial potential effective usage.

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