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FINANCE

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The essence and functions of finance and financial relations, the monetary system of the country, the financial policy, state and local budgets, tax regulation of the economy, peculiarities of functioning of the financial market and the insurance market, as well as the mechanisms of regulation of financial activity of economic entities regardless of their size and type of ownership have been given consideration.

For foreign students of speciality 072 "Finance, Banking and Insurance".

UDC 336(075)

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Content

Introduction

Finance is a part of the market economy and the instrument by which the government implements its functions, regulates economic processes to ensure political and economic stability and social development of all sectors of economic activity. Deep understanding of the nature of financial and credit relations, principles and mechanisms is obligatory for successful professional activity. Finance is the branch of knowledge that deserves careful study because of its importance for general education of students as well as one of the basic educational disciplines in the curriculum of bachelors of science in economics.

The aim of the academic discipline "Finance" is to form integrated knowledge of finance theory, patterns of its functioning at the meso-, macro- and microlevels as the basis of the state financial system development.

The subject of the academic discipline is economic relations concerning the formation, distribution and use of centralized and decentralized monetary funds.

To succeed in learning the academic discipline "Finance" it is important to have basic knowledge and skills in macro- and microeconomics, money and credit, economic statistics, business economics.

The textbook consists of ten topics according to the syllabus of the academic discipline. Each topic includes a brief description of the main issues, questions for self-assessment and practical tasks with guidelines to them.

The textbook material aims to help students master the terms and concepts of the academic discipline and gain practical skills in the use of its main instruments. This discipline is basic for bachelor's degree students of speciality "Finance, Banking and Insurance" who are foreigners and who are not fluent enough in Ukrainian or Russian. As a result of learning the academic discipline students should form professional, objective and cognitive competences in finance.

Topic 1. The essence of finance and the subject of financial science

The aim is to form a comprehensive understanding of the activities of the state, business entities, organizations and individuals associated with the creation and use of financial resources, learning the essence of the science about finance and the toolkit for research into finance, the genesis of its appearance and development.

The main issues

1.1. The object and the aim of financial science.

1.2. The methods and components of the science about finance.

1.3. The historical aspects of the financial science formation and development.

1.4. The development of financial science in Ukraine.

The competences to be formed:

knowledge:

definition of the economic category "financial science";

methods and components of financial science;

the main historical aspects of the financial science development;

study of Ukrainian scientists' contribution to the financial science formation and development;

skills:

to define financial science as a science which studies the phenomena and processes that are implemented by the state during the creation and use of financial resources for economic and social development;

to determine the subject of financial science;

to argue methods of scientific knowledge used in financial science;

to identify and analyze the stages of formation and development of financial science;

to determine and argue the features and periodization of the financial science development in Ukraine;

communication:

the ability to identify the core elements of financial science;

the ability to identify the key elements and stages of the financial science development;

autonomy and responsibility:

definition of the system characteristics of financial science;

definition of features and rules of financial idea in Ukraine.

Key words: financial science, financial mind, financial relations, financial theory, financial knowledge, the study about finance.

1.1. The object and the aim of financial science

Financial science is a branched and differentiated system of knowledge about financial phenomena and processes, their organization and systematization in the context of a certain paradigm, with the identified valid backgrounds of their appearance, mechanisms and principles of functioning, provable, reasonable ideas and conclusions about their impact on people, economy, society, civilization, evaluation of achievements, gains, losses [5] (Fig. 1.1).

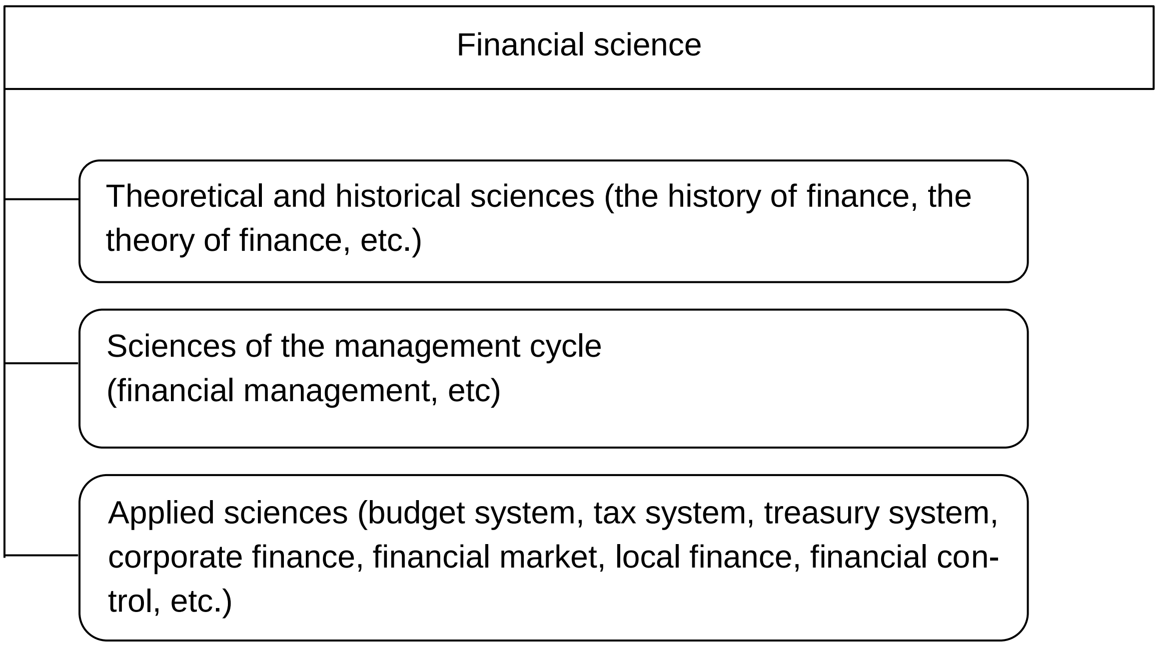

Fig. 1.1. **Financial science as an area of scientific knowledge**

There are three manifestations of financial science in the socio-historical realities [40], namely:

as a certain complex of knowledge and information about finance;

as an activity related to the development of knowledge about finance;

as a complex of groups, institutions, agencies, and departments that ensure the implementation of financial research activity.

Financial science performs both general scientific and specific scientific functions (Table 1.1)

Table 1.1

The main functions of financial science

Type	The content
1	2
The general scientific functions	
The epistemological (cognitive) function	Providing the society with the necessary knowledge about finance for the right problem solution, in particular the theoretical representation of finance at the level of general laws of its emergence, development and operation
The function of social memory	Accumulation, saving, translation of the experience of finance operating in the previous historical periods
The function of interpretation	Explaining the nature of finance and financial phenomena, their causality, structural organization, public use
The function of forecast	Determining the prospects of finance development which are based on the identified patterns and trends of finance and financial system by forming hypotheses, predictions, analysis of various options and alternatives
The heuristic function	Though similar to the informative function, this one, unlike it, does not mean theoretical perception of reality and expansion, systematization of the available financial knowledge, but implies identification of new, previously unknown properties of finance and financial phenomena
The regulatory function	Establishing, organizing and regulating the relations between scientific entities with relevant standards and rules of ethics
The ideological function	Affecting the development of social ideology. In particular some financial phenomena and ideas are parts of social ideology, which fix the universal values and ideals and reflect the interest and wishes of certain social groups and are used for the compilation of party programs, basic principles of domestic and foreign policy, etc.
The educational function	Providing financial education of various segments of population, formation of certain financial benchmarks and financial literacy of different society members
The communicative function	Interconnection and interaction of all types of financial science, the improvement of financial knowledge, the use of knowledge of other branches of science by financial science, avoiding duplication of research and gaps in the financial sphere, overcoming unhelpful and unnecessary discussions through the use of scientific language as a clear and important means of communication

Table 1.1 (the end)

1	2
The applied function	Contribution to the solution of practical tasks of social and economic transformation through the development of practical solutions to financial issues, projects of regulations on finance, concepts of the public financial institutions' reform, etc.
The creative function	Creation of powerful intellectual potential of financial scholars
Special functions of financial science	
The financial orienting function	Determining benchmarks, values, ideas and principles, ways to improve financial relations and financial legislation, financial regulation, financial support, creation of a reliable financial mechanism, etc.
The instrumental function	Determining the value of financial science as a tool of society and state as for the scientific support of financing
The critical and expert function	Critical understanding of the theoretical principles of financial science and practices, the state of financial legislation, organization and operation of the financial apparatus of society, their compliance with the norms and democratic principles, scientific expertise of various financial projects and regulations

The object of financial research is a process or phenomenon of financial theory and practice that generates a problem situation and is chosen for further learning.

The objects of financial science are:

funds (centralized: state and local budgets, the Pension Fund of Ukraine, the state social funds, state reserves, state loans; decentralized: funds and reserves of the ministries, departments, central agencies, departments and offices of local and state authorities, executive committees of local councils, enterprises, organizations and institutions of all forms of ownership);

capital and financial resources of society, state, businesses, administrative and territorial entities;

income and savings (revenues from sales of goods and services, income and revenues from other activities, profits, depreciation, etc.);

specific types of taxes, obligatory fees, non-tax revenues to the budget;

all kinds of costs;

all kinds of financial plans and their indicators, etc.

The subject of financial science is a set of financial relations at different stages of distribution and redistribution of the GDP, different levels of economic system, between different actors of relations, the economic base of which is the movement of value in monetary form.

The actors of financial relations are state, state authorities of different levels, an enterprise, its units, public organizations, members of society [5] (Table 1.2).

Table 1.2

The actors and forms of financial relations

The actors of relations	The form of financial relations
State and enterprise	Payments to the state budget
	Deductions to various funds of state, regional and industrial levels
	Financial support of state enterprises and organizations from the state budget
Enterprises	Payment obligations of suppliers and buyers
	Penalties for violation of the contractual discipline
	Financial rewards for implementation of special customer requirements
Enterprise, its units and employees	Providing of economic relations
	Monetary remuneration of employees
State authorities at different levels	Distribution of differential rent
	Financing of environmental protection, etc.
	Financing of regional clusters
State, cooperative and private enterprises, state, organizations and institutions	The system of taxation and economic exemption
	Budgetary financing
	The tax system
State and population	Pensions, benefits, scholarships, payments from public funds of consumption, taxes
Banking, commercial institutions and population	Lotteries, contributions to savings and other banks, consumer credit, insurance, buying/selling of financial assets, etc.

Financial science is a highly branched system of scientific knowledge, types and forms of scientific activities. Each structural part (branch) is based on the needs of cognitive and practical financial activity and demonstrates the multidimensional and multipurpose function of finance as a separate science.

1.2. The methods and components of the science about finance

Financial science as a system is formed by interconnected blocks of the scientific financial knowledge (Fig. 1.2).

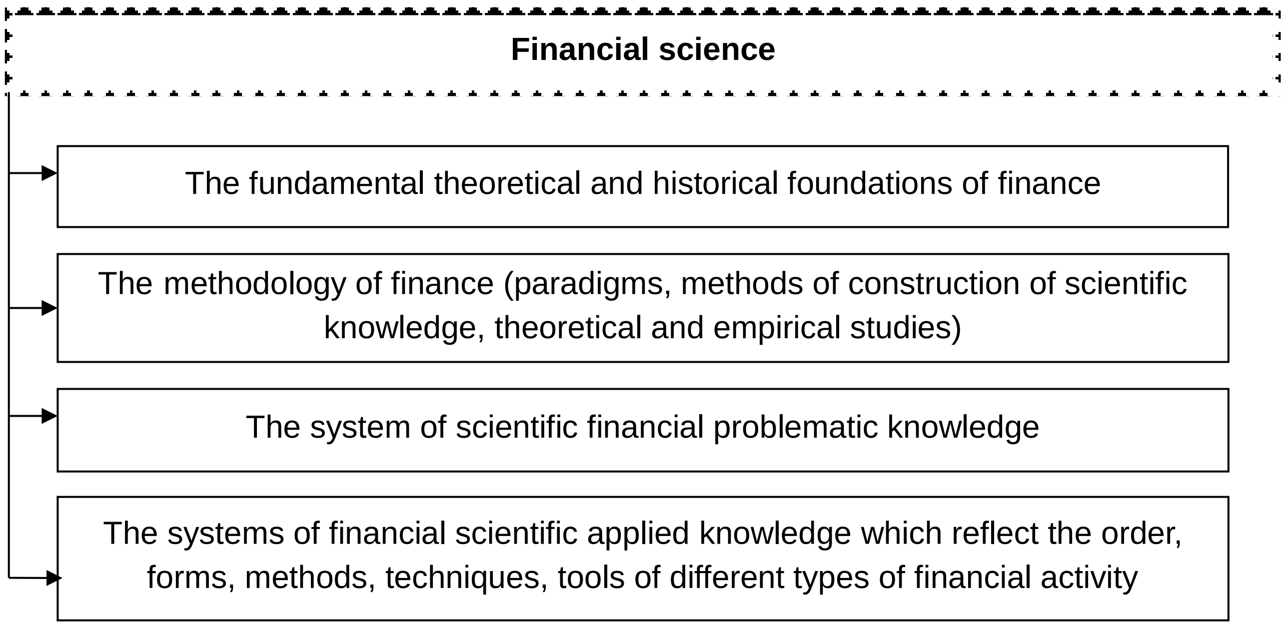

Fig. 1.2. **The structural components of financial science**

The components of the scientific financial knowledge system

Financial theory is a complex of facts and explanations of these facts united by a single internal cognitive logic, interconnected in its parts, accumulated by certain time.

Financial science is a regularized process of knowledge, its organization and systematization in the light of a certain paradigm, such as the amount of knowledge about the phenomena of international, public and private finance and a set of operating rules.

Financial mind is an intellectual process at any stage of the cognition of financial phenomena and with any result from the hypothesis to the reliable knowledge. Financial mind works equally for financial theory and financial science.

The functions of financial theory

1. The explanatory function reveals patterns of the financial theory subject development, scientific rationale of these patterns.

2. The predictive function makes it possible to determine trends in the development of financial phenomena and processes, to predict future events.

3. The synthesizing function reveals the natural connections between different parts and elements of the theoretical framework which gives an opportunity to define fundamentally new integration qualities inherent in financial theory as a holistic system in contrast to separate parts and elements.

4. The methodological function manifests itself in the fact that under certain conditions, financial theory after some relevant changes turns into a cognition method, but the individual methods of financial research acquire qualities of financial theory and theoretical values.

5. The practical function points at the application of financial theory, because the development of theory is not the goal of financial science [5].

1.3. The historical aspects of the financial science formation and development

History shows that financial science had not existed separately for a long time. Like most economic sciences finance began to develop as a part of economics. The science of finance, like the majority of the most important sciences, emerged from practice. The emergence of financial practices was a millennium ahead of financial science. Firstly, there were many financial economies that evolved, expanded, and then failed, but knew nothing about financial science. Financial science appeared much later with a number of other socio-political sciences.

The formation and development of financial science in retrospect are given in Table 1.3 [1; 5].

Table 1.3

The formation and development of financial science in retrospect

The period	The name of the stage	The characteristic of the stage	The direction in economic theory	The main representatives
1	2	3	4	5
The ancient times BC	The unscientific period	Financial science had only aesthetic character. The existence of a state provided for the collection of taxes and spending of its main part on the security and infrastructure, to which the fragments of scientific work were devoted to	–	Xenophon, Aristotle, Plato
The middle ages	The transition to the scientific process	Financial science is almost nonexistent due to insufficient development of the financial sector. Nevertheless, the representatives of scholasticism actively contributed ideas about the right of a state ruler to use taxes only for common interests	Scholastic	Thomas Aquinas, F. Petrarch
15 – 16th centuries	The emergence of financial science. The strengthening of financial science and financial practices	The fixation of a link between financial theory and practice: the science becomes more influential in financial practices. The main problem of theory is the definition of methods for the enrichment of nation for the purpose of economic development. The macroeconomic category "national wealth" as a common good necessary for the state was introduced in scientific circulation. The sphere of circulation (primarily external and internal trade and monetary circulation) has become the subject of theoretical research. The category of capital was entered and the necessity for accumulation of capital was proved. Financial science exists as a component of the general theory of political economy	Monetarism (early mercantilism), mercantilism	C. Carafa, F. Guicciardini, M. Palmieri, G. Botero, N. Machiavelli, J. Schumpeter, M. Luther, J. Calvin, J. Bodin, A. de Montchrestien

Table 1.3 (continuation)

1	2	3	4	5
17th – beginning 18th centuries	The activation of financial mind	The sharp need of the states of Western Europe for taxes intensified financial mind. Financial science developed with the emergence of the doctrine of taxes. The reasons and ways to reduce the burden of taxation were analyzed. The approaches to taxation were studied. The financial sector was researched by the state. Financial science existed as a component of the general theory of political economy. The dominant financial views were systemized	The birth of classical political economy	W. Petty, T. Hobbes, J. Locke, F. Justi, J. Necker, J. Sonnenfels, S. Pufendorf, etc.
18th century	The formation of a common system of financial science	Financial phenomena were attached to the field of political economy, contributed to their further scientific development. Physiocrats created the theory of tax diversification. The doctrine of profit reasoned further development of important questions of land rents and income has made a significant contribution to the analysis of differences and perspectives of direct and indirect taxation. Financial science existed as a component of the general theory of political economy	Physiocracy	D. Keune, A. Turgot, H. Mirabeau
The end of the 18th – middle 19th cent.	Separation of financial science as an independent scientific discipline	Financial science was provided with fundamental political economic base. The basic issues of financial science – taxes, budget, public debt, loans, etc. were developed. The research on finance nature in capitalism was undertaken. Financial science existed as an independent branch of science and was not a part of political economy	The heyday of classical political economy, (vulgar political economy, Marxism). Cameralism	A. Smith, D. Ricardo, J.-B. Say, T. Malthus, N. Senior, J. Mill, K. Marx, F. Engels, L. Stein, A. Schäffle, etc.

Table 1.3 (the end)

1	2	3	4	5
Beginning of the 19th – beginning of the 20th century	Formation of a new paradigm of financial science	The conclusions of the theory of marginalism made it possible to form a general construction of financial science and analysis of an entity of separate financial phenomena and institutions, first of all the phenomenon of transcriptions of taxes according to the theory of marginal utility. The quite holistic theory of public finance was created. The public policy of financial and economic crisis was determined. The fundamentally new theory of finance was developed. It was aimed at regulating the economy in terms of the production monopolization	Neoclassical theory of finance (marginalism), Keynesianism, neoliberalism	W. Jevons, C. Menger, E. Bohm-Bawerk, N. Wieser, A. Stewart, L. Mises, F. Hayek, F. Liszt, A. Wagner, G. Schmoller, M. Weber, K. Ditzel, W. Sombart, A. Marshall, J. Keynes, etc.
20th century	Modern development of financial science	The quantitative relationships between financial performance, deficit financing, cyclic regulation of economy were studied. The concept of equilibrium of economy under conditions of underemployment, which imposed a monetary factor was formed. Theoretical understanding was reached and the rationale of the role and mechanisms of interaction of capital markets and the largest national and multinational corporations in national and international financial relations was founded. The theoretical understanding of the role of finance as a main system forming cells of any economic system-entity's level was provided	Newkensington, post keynesian, neoclassical theory, monetarism	E. Hansen, A. Okun, W. Heller, W. Schultz, S. Harris, R. Lindholm, O. Eckstine, R. Harrod, A. Peacock, J. Weisman, F. Perroux, F. Neumark, P. Arestis, P. Samuelson, J. Schumpeter, etc.
The end of the 20th – 21st centuries		Financial relations in the context of asymmetric information, institutions as a special form of social life and human relations, social insurance, transaction costs were studied	The theory of information asymmetry, institutionalism	G. Akerlof, V. Spens, W. Mitchell, D. North, R. Kous,J. Buchanan, M. Olson, O. Williamson

So, after consideration of the financial science history, it can be argued that the ideas put forward by scientists of the past centuries, were further developed in modern theories and concepts.

1.4. The development of financial science in Ukraine

Financial science in Ukraine was formed later than the other economic sciences (the formation of its doctrine took place at the beginning of the 19th century, the heyday was at the end of the 19th and beginning of the 20th century) but already in the 19th – early 20th century it had the brightest representatives with ideas recognized globally. Their certain achievements have not lost relevance nowadays. They are the foundation of our country's financial school [5].

The stages of the Ukrainian financial mind evolution are described in Table 1.4

Table 1.4

The stages of the Ukrainian financial mind evolution

The qualitative characteristic of the financial science development	The historical period	The sources
Emergence of financial mind	16 – 18th cent.	The works of thinkers, historical documents
Formation of financial science	1st half of the 19th cent.	Government reforms, projects, monographic researches
Development of financial theory	2nd half of the 19th – beginning of the 20th cent.	Training courses of policy and financial law, political economy, the basics of financial science, monographs, scientific journalism
Destruction of financial science	1930 – 1970	Party and state documents, textbooks, scientific publications
Formation of modern concepts	1980 – nowadays	Monographic researches, educational literature, publications in scientific journals

Accelerating globalization of the world economic processes, increasing transformation of domestic economy into the financial economy set new challenges to the Ukrainian financial science. A qualitative leap should be taken in the formulation of scientific foundations of the structural and institutional reforms in the financial sector that will meet the latest requirements of socio-economic development of the country and the challenges of the European geofinancial environment. At the same time it is necessary to raise the level of financial literacy of the society – understanding the starting positions of the finance functioning should become an absolute necessity for every educated person.

Questions for self-assessment

1. What is financial science?
2. Name and explain the main functions of financial science.
3. Describe the objects of financial science.
4. Who can be participants of financial relations?
5. What is the difference between financial theory and financial mind?
6. What are the stages of the Ukrainian financial mind evolution?

Seminar topics

1. Development of financial science in the middle ages (the transition to the scientific process): Thomas Aquinas, F. Petrarch.

2. The emergence of financial science. The strengthening of financial science and financial practices (15 – 16th cent.): C. Carafa, F. Guicciardini, M. Palmieri, G. Botero, N. Machiavelli, J. Schumpeter, M. Luther, J. Calvin, J. Bodin, A. de Montchrestien.

3. The activation of financial mind at the end of the 17th and at the beginning of the 18th centuries: W. Petty, T. Hobbes, J. Locke, F. Justi, J. Necker, J. Sonnenfels, S. Pufendorf, etc.

4. The formation of a common system of financial science (18th cent.): D. Keune, A. Turgot, H. Mirabeau.

5. Separation of financial science as an independent scientific discipline (the end of the 18th – middle 19th cent.): A. Smith, D. Ricardo, J.-B. Say, F. Bastiat, T. Malthus, N. Senior, J. Mill, K. Marx, F. Engels, L. Stein, A. Schäffle, etc.

6. Formation of a new paradigm of financial science in the 19th – beginning of the 20th cent.: W. Jevons, C. Menger, E. Bohm-Bawerk, N. Wieser, A. Stewart, L. Mises, F. Hayek, F. Liszt, A. Wagner, G. Schmoller, M. Weber, K. Ditzel, W. Sombart, A. Marshall.

7. Peculiarities of financial science of the 20th century: E. Hansen, A. Okun, W. Heller, W. Schultz, S. Harris, R. Lindholm, O. Eckstine, R. Harrod, A. Peacock, J. Weisman, F. Perroux, F. Neumark, V. Wittmann, G. Haller, J. Robinson, P. Arestis, P. Samuelson, J. Schumpeter, M. Friedman, etc.

8. Modern development of financial science: G. Akerlof, V. Spens, W. Mitchell, D. North, R. Kous, J. Buchanan, M. Olson, O. Williamson.

9. Evolution of the Ukrainian financial mind.

Topic 2. The genesis and evolution of finance

The aim is to create a comprehensive view, a system of knowledge and practical skills for the interpretation of financial categories, financial relations, the order of centralized and decentralized funds forming in the process of the distribution and redistribution of national income.

The main issues

2.1. Finance as an economic category.

2.2. The social and economic essence and functions of finance.

The competences to be formed:

knowledge:

the essence of financial relations and finance;

groups of financial relations;

the functional purpose of finance as an economic category;

skills:

analysis and characterization of the background for the emergence and development of finance depending on the specific historical forms of economic relations;

the definition of the economic content, the socioeconomic value and specific features of finance;

communication:

the ability to identify the core elements of financial relations;

the ability to define financial relations in the entire set of monetary relations;

autonomy and responsibility:

determination of the genesis and the evolution of finance patterns depending on the specific historical forms of economic relations.

Key words: finance, financial attitudes (relations), financial resources, primary income, secondary income, funds, money.

2.1. Finance as an economic category

The backgrounds of the definition of finance [6; 12]:

Firstly. In Central Europe, after the first bourgeois revolutions monarchical regimes were changed. The power of the monarchs was significantly reduced. It is most important that the head of a state (monarch) was rejected from the Treasury. The nationwide fund arose. The head couldn't use this budget single-handedly.

Secondly. Systemic formation and use of the budget led to the emergence of the government revenue and expenditure systems. They were characterized by a specific composition, structure, and legislative fixation. The main groups (parts) of expenditure budget remained almost the same for many centuries. At that time, four directions of expenditures were identified: for military purposes, management, economy, social needs. Another interesting fact is that the share of management costs was practically still the same (11 – 13 %) in the budgets of different countries in different periods.

Thirdly. Taxes in the monetary forms became prevalent, whereas previously the state income was formed mainly by the natural taxes and labor obligations. Thus, only at this stage of the statehood and cash nexus development distribution of a new product in the cost terms became possible.

The main causes of finance are:

1. The deepening of public labor division as a result of logical development of public production relations.

2. The spread of commodity-money relations; the need for the distribution and redistribution of the gross domestic product (GDP) for the purpose of keeping the reproduction proportions.

3. The maintenance of non-productive areas, management, national defense and so on.

2.2. The social and economic essence and functions of finance

Finance is economic relations that arise in the process of distribution and redistribution of the GDP value or/and a part of national wealth at the macrolevel, as well as income or profit at the microlevel, in connection with formation of funds by business entities or state and use of these funds for extended reproduction, employee financial incentives, meeting social and other needs.

The features of finances:

the exchange and distributive nature;

the movement of value from one entity to another;

the monetary form of relationship;

income generation and expenditure;

the exchange is equal to the distribution (by their mission) but unequal to redistribution.

The role of finances in society is:

to provide the distribution of the GDP and financial needs of legal entities, individuals and state;

to provide the circulation of financial resources and, as a result, the continuity of reproduction;

to implement the redistribution of primary and secondary income between industries, regions, social strata, separate legal entities and individuals;

to affect the interests of the subjects of distributive relations and regulate various areas of socioeconomic development;

to play a leading role in the system of the country economic management;

to form a system of financial indicators which serve as indicators of the status and development of economic and social public areas;

to provide comprehensive control between the subjects of the exchange and distributive relationship for financial resources formation and use.

Finances implement four basic functions (Fig. 2.1).

The distributive function of finance. The redistribution of national income (NI) has the following reasons: the cross-industry and territorial redistribution of funds; the presence of production and nonproduction spheres; the presence of different social groups; the presence of various forms of ownership [37; 44].

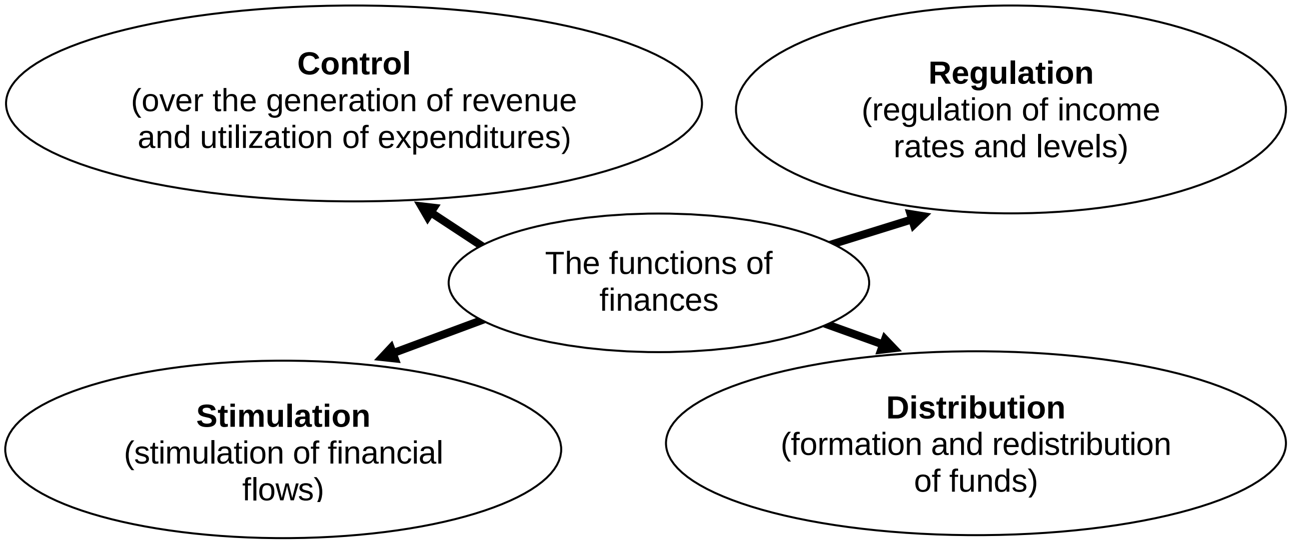

Fig. 2.1. **The functions of finances**

The objects of distribution are:

the GDP i.e. the value of final products (goods) produced by society during a certain period of time (mostly a year);

national wealth – the sum of created and accumulated benefits owned by society and natural resources involved in economic turnover;

external receipts in the form of financial help, foreign government loans, foreign investment and other intergovernmental transfers from foreign countries, international financial institutions and foreign legal entities and individuals.

The subjects of distribution are: the state; legal entities (economic entities of various forms of ownership, level of subordination and location); households and individuals; international organizations; other countries.

The links of the financial system that serve different types of financial distribution: *intraeconomic* – between enterprises' finance; *cross-industry and cross-territory* – between the state budget, or target state funds.

Primary distribution – primary income is divided into two groups:

1) salary of workers, employees, the income of farmers engaged in the material production;

2) the enterprise's profit in material production.

Secondary distribution – secondary income is the income received in nonmanufacturing industries (budget sector): education, healthcare, science, law enforcement, defense, etc. Secondary distribution is the final stage of the implementation of the distribution function of finance. It involves the use of state funds for the development of priority sectors of the economy, sociocultural activities, social protection, defense, management and others.

The control function of finances. Its tasks are:

the timely implementation of financial obligations to the entities, budget, banks;

the mobilization of financial resources needed for the industrial and social development;

the equity increase;

the effective target distribution and the use of financial resources [40].

The object of financial control is the financial activities of business organizations, public institutions and organizations engaged in financial activities. The subject of control is financial transactions associated with the creation and use of financial resources.

The types of financial control:

nationwide, carried out by state bodies (Tax Authorities, Treasury, Audit Departments, Ministry of Finance, etc.);

intraeconomic, provided by financial services of companies and institutions;

independent, provided by audit firms.

The regulatory function of finances. The direction of the function is the socioeconomic processes in a society that occur under the influence of market relations. A condition for the realization of the function is the need for a change in the distribution of funds for the maintenance of normal reproductive processes regardless of the level and place.

The stimulation function of finances. The main tool of influence is taxes. The subjects of stimulation are enterprises, organizations and legal entities that are engaged in economic activities. The object of stimulation is economic activity, which is aimed at the increase of the GDP. The forms of stimulation are the fixation of different tax rates, tax exemption for certain entities and narrowing the tax base.

Questions for self-assessment

1. What is the main purpose of finance?
2. Describe finance as an economic category.
3. Name four stages of public reproduction. At what stages does finance exist?
4. Give the definition of the category "finance".
5. Describe the role of finance in society.
6. Name the functions of finance.
7. Explain the essence of the control and simulative functions of finance.

Practical tasks

Task 1. Imagine the following situations.

Situation 1. You are on your own land digging a ditch with your own shovel.

Situation 2. Having your own land you need to dig a ditch in it. You hire a worker who will receive a wage for his work, and the ditch will be your ownership.

Situation 3. You don't have time to deal with your land. You lease it for 10 years. The tenant has been using your land for 10 years at his own discretion.

Situation 4. Everything is similar to situation 3, but the tenant does not work himself, he hires workers who carry out his projects.

Task 2. Concerning each situation, identify who is: the owner, the user of the land, the owner of the product of labour (fill in Table 2.1).

Table 2.1

Situation	The owner of the land	The user of the land	The owner of the product of labour
1			
2			
3			
4			

Task 3. Using Table 2.2, determine the GDP and the NI of the country with costs and income.

Table 2.2

Indicator	**Actual prices, billion UAH**
Export	2200
Total dividends	300
Depreciation	1000
Total salary	4500
State expenditures	2800
Rent	500
Indirect taxes	1600
Net investments	800
Transfer payments	2300
Interest on capital	900
Property income	200
Consumer spendings	6500
Import	3300
Profit tax of corporations	400
Retained income of corporations	600

Methodical recommendations

Cost-based GDP = consumer spendings (C) + total investments (I) + + state expenditures (G) + net export (X_n).

Income-based GDP = total salary + rent + interest on capital + revenue (property income + profit tax of corporations + total dividends + retained income of corporations) + depreciation + indirect taxes.

NI = GDP − depreciation − indirect taxes.

Topic 3. Financial law and financial policy

The aim is to form knowledge and ability for logical understanding of the essence of financial law and state financial policy, of tools and forms of financial policy and to develop practical skills concerning the evaluation of its effectiveness.

The main issues

3.1. Financial law: the subject, methods and relationship with other branches of Ukrainian law.

3.2. The content, purpose, and objectives of financial policy.

3.3. The components of financial policy.

3.4. The nature and components of the financial mechanism.

The competences to be formed:

knowledge:

the basics of financial law and financial policy;

the types and components of financial policy;

skills:

to analyze and use the methods of financial law;

to determine the features and main components, types of the state's financial policy;

communication:

the ability to identify the core elements of financial law and financial policy;

the ability to implement the basic principles of financial policy functioning;

authority and responsibility:

to define features of financial law and financial policy in Ukraine.

Key words: financial law, financial policy, state financial activity, state funds, fiscal policy, monetary policy, spending multiplier, multiplier, internal stabilizers, financial restriction, financial expansion.

3.1. Financial law: the subject, methods and relationship with other branches of Ukrainian law

Financial law is a set of legal rules regulating social relations in the sphere of formation, distribution and use of centralized and decentralized funds of a state and its territorial communities.

The subject of financial law is financial relations that take place in the formation, distribution and use of state and local budgets, special trust funds; taxation, state and municipal credit, budgetary financing, financial control, obligatory state insurance, money turnover, payments, banking regulation and supervision, currency regulation [25].

The object of financial relations is the funds that are generated, distributed and used through the implementation of subjective rights and legal duties of participants in financial relations. The object of financial relations will always be linked with the interest of the state.

The participants in financial relations are the following:

1. The state which acts in the person of the entitled body of state power or local government. These are the bodies of general competence – the Verkhovna Rada of Ukraine, the Cabinet of Ministers or special competence in financial sphere – the State Treasury, the State Tax service of Ukraine, the National Bank of Ukraine and the like.

2. Legal entities and individuals which fulfill their legal responsibilities and contribute to the mobilization and use of financial resources (enterprises, organizations, citizens, public institutions).

Financial legislation is a set of normative acts that contain norms of financial law.

The sources of financial law in Ukraine are*:* the Constitution as the basic law of Ukraine; general and special laws; decrees of the Verkhovna Rada of Ukraine; decrees of the President of Ukraine; decrees of the Cabinet of Ministers of Ukraine; departmental legal acts (resolutions of the Board of the NBU); orders of the Minister of Finance; instructions of the State Treasury of Ukraine, etc.); international legal acts, customs and standards ratified by the Parliament that form a part of national law.

3.2. The content, purpose, and objectives of financial policy

Financial policy is a complex of actions and measures undertaken by a state within the limits of its functions and powers in the sphere of financial activities of business entities and financial institutions, citizens and state for the purpose of carrying out specific tasks and achieving goals [98].

The content of financial policy is the development of the main ways to use finance based on the need for economic and social problem solving.

Through financial policy, the government finances the needs of expanded reproduction, adjusts the scale and proportions of the social production development, improves its local and territorial structure.

Financial policy is implemented by financial authorities and institutions. The object of financial policy is formation, allocation and use of the financial resources. The means of financial policy implementation is the financial mechanism.

The principles of state financial policy are: scientific validity, consistency, target orientation, continuity, availability, the balance of revenues and expenditures in all areas of financial system, contribution to the production, maintaining business activity and raising employment, creation of financial reserves, search and continuous improvement of the forms and methods of mobilization and use of financial resources [45].

The important objectives of financial policy are:

providing conditions for mobilization of financial resources at the minimum required size;

optimal distribution and rational use of financial resources;

regulation and financial incitation of socioeconomic development;

development of the financial mechanism in accordance with the realities of market economy;

creation of an effective system of financial management.

According to the stages of state development, three types of financial policy can be distinguished. They are classic financial policy, regulatory financial policy, planning financial policy.

The basis of classic financial policy is the interference of the state in the economy, the preservation of free competition, the use of the market mechanism as the main regulator of economic processes. This policy leads to the limitation of public expenditures and taxes, provides conditions for a balanced budget formation and execution.

3.3. The components of financial policy

The financial strategy is the main directions of the finance long-term use. The financial strategy is reflected in future plans. The process of its development includes the prediction of major trends in finance development, the formation of the concept of the use of these trends, the determination of the principles of the financial relations management.

Financial tactics aims to solve the problems of a specific stage of society development through the exemptions providing or reducing promotion or limitation of certain activities [5].

In Table 3.1 the forms of state financial policy are given.

Table 3.1

The forms of state financial policy

Criterion	Form	Characteristic
1	2	3
Components	Fiscal policy	Governmental measures aiming to provide full employment and non-inflationary GDP by changing governmental spendings, tax system and approaches to the state budget formation
	Monetary policy	A set of measures in the sphere of money turnover and credit, aimed at the regulation of economic growth, inflation control and stability of the monetary unit of Ukraine, employment and alignment of the balance of payments

Table 3.1 (the end)

1	2	3
Level of implementation	Financial policy of the state (macro level)	An integral part of economic policy that covers a set of measures which the state provides at all levels of management concerning finance organization and use to implement its functions and solve the urgent specific problems
	Financial policy of business entities (micro level)	The purposeful use of funds to achieve long-term and short-term objectives
	Financial policy of international organizations and financial institutions (international level)	A set of measures and governmental recommendations in the area of international finance, issued in the norms and principles of international financial law
Goals to be achieved by financial policy	Stabilization policy	Maintaining macroeconomic balance through the production volume with price stability. Its implementation is based on stable financial resources ensuring constant proportions of distribution and redistribution of the income received
	Economic growth policy	Achieving the necessary level of the annual GDP growth; extending and ensuring the availability of financial resources

3.4. The nature and components of the financial mechanism

The financial mechanism is a combination of economic, organizational and legal forms and methods of state financial management in the process of creation and use of financial resources to meet the needs of state bodies, business entities and population [5].

Financial methods are the ways of influence on the economic relations by special financial tools. They operate in two directions: along the line of control of the movement of financial resources and market commercial relationships associated with comparison of costs and benefits, the responsibility for the effective fund usage.

Financial tools are the instruments for managing the formation and distribution of centralized and decentralized financial resources.

The main tools are: financial norms, standards, limits, reserves, incentives.

The financial mechanism is given in Fig. 3.1.

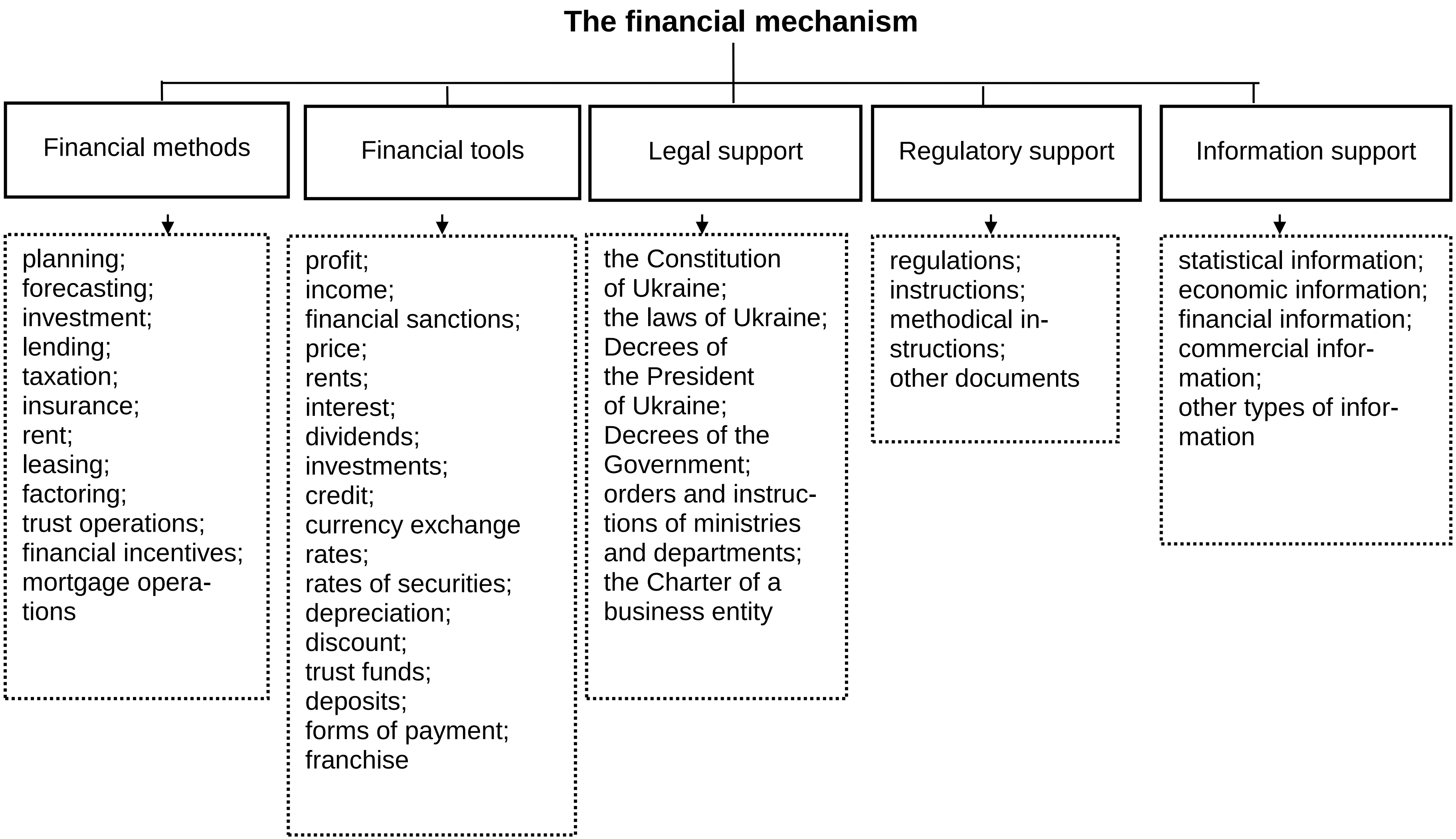

Fig. 3.1. **The financial mechanism**

Questions for self-assessment

1. What is financial law?
2. Name the objects of financial relations.
3. Identify the major participants in financial relations.
4. Name the sources of the Ukrainian financial law.
5. Give a definition and explain the purpose of the state financial policy.
6. What are the principles of the state financial policy?
7. What types of state financial policy exist in the world practice?
8. What types of financial policy are used by Ukrainian government?
9. Describe the elements of the state financial mechanism.

Practical tasks

Task 1. The Verkhovna Rada of Ukraine adopted a balanced budget for 2014. Government expenditures (G) and taxes (T) at the same time increase by 1 billion UAH. The marginal propensity to consume is 0.75. Determine the impact of the balanced budget on the real GDP of Ukraine in 2014.

Methodical recommendations

Conducting a discretionary fiscal policy involves deliberate manipulation of taxes and government expenditures to achieve the potential national production and full employment, inflation control and economic growth acceleration.

The budget is balanced if government expenditures are balanced with revenues from taxes, or their changes are also balanced ($G = T$ or $\Delta G = \Delta T$).

1. Let us determine the change in the real GDP (ΔGDP) due to the increase in government expenditures by 1 billion UAH. It occurs because of the multiplier of government expenditures (m_g).

The multiplier of government expenditures shows how many times the income increases when state expenditures increase by 1 unit of a product. This multiplier has the following form:

$$m_g = \frac{\Delta Y}{\Delta G} = \frac{1}{1 - MPC} = \frac{1}{MPC}; \quad (3.1)$$

$$\Delta Y = \Delta G \times m_g, \quad (3.2)$$

where *MPC* is the marginal propensity to consume (the ratio of the consumption runup to the income runup);

MPS is the marginal propensity to save (the ratio of the saving runup to the income runup).

For example, if the state increased its expenditures by 100 UAH, it has created an additional income (ΔY) to some economic entity which equals 100 UAH from which it spends 80 UAH on consumption (ΔC) and 20 UAH on savings (ΔS). Then *MPC* = 0.8, while *MPS* = 0.2.

The entity that has acquired 100 UAH as additional income, will spend 80 UAH and create an additional income for another economic entity from which that entity will spend 64 UAH (80 × 0.8 = 64) on consumption and 16 UAH (80 × 0.2 = 16) on savings and so on.

2. The next step is estimation of the influence of taxes on the change in the real GDP which is realized with the multiplier of taxes (m_{Tx}).

The multiplier of taxes is the indicator which shows how many times the total income will increase (decrease) if taxes increase (decrease) by 1 unit. It is negative because of the opposite effect on the total income. Its absolute value is lower than the multiplier of expenditure:

$$m_{Tx} = \frac{-MPC}{1-MPC}. \quad (3.3)$$

Taxes influence the total income through the change of consumer incomes, that is why:

$$\Delta Y = \Delta T_X \times m_{Tx}. \quad (3.4)$$

3. The final step involves estimation of the influence of the balanced budget on the GDP of Ukraine in 2014. The multiplier of the balanced budget (m_{BS}) should be used:

$$m_{BS} = m_g - m_{Tx}. \quad (3.5)$$

m_{BS} shows that the equal runups of government expenditures and taxes lead to the increase of production by the figure of expenditures and taxes.

If government expenditures (*G*) and taxes (*T*) increase by the same figure, then the balanced level of production increases by this figure too.

Topic 4. Taxes. The tax system

The aim is to form a comprehensive understanding of the taxes and fees in Ukraine, the components of the tax system and its influence on the economy of the country.

The main issues

4.1. The socioeconomic essence of taxes and their functions.

4.2. Taxation elements. Classification of taxes.

4.3. The essence of the tax system and the principles of its construction.

The competences to be formed:

knowledge:

the fundamentals of the taxation system and its importance for public distribution of the total product;

the principles and structural elements of the tax system of Ukraine;

skills:

identification and analysis of the tax burden in the state;

identification and analysis of the tax base;

calculation of taxes and obligatory payments;

filling in tax declarations and calculation of the single social tax for different categories of taxpayers;

communication:

the ability to define the essence of taxes and the tax system;

the ability to analyze the main factors that affect the process of taxation and the tax system;

autonomy and responsibility:

understanding the mechanism of the tax system functioning;

determination of the optimal rates of taxes;

definition of the factors influencing the national tax system.

Key words: taxes, obligatory payments, tax burden, tax base, tax system, tax benefit (exemption, concession), exemption limit, minimum salary.

4.1. The socioeconomic essence of taxes and their functions

Taxes are payments of legal entities and individuals which are levied to the state budget (state and local) and government target funds.

A fee is a payment for the possession of a special right.

A duty is a payment for some kind of state service.

The biggest difference between taxes and other obligatory payments is that: instead of other obligatory payments which are charged to the funds of obligatory social insurance, taxes don't have clear direction [24; 26]. All other payments are not permitted to be used for other purposes. The features of taxes are presented in Fig. 4.1.

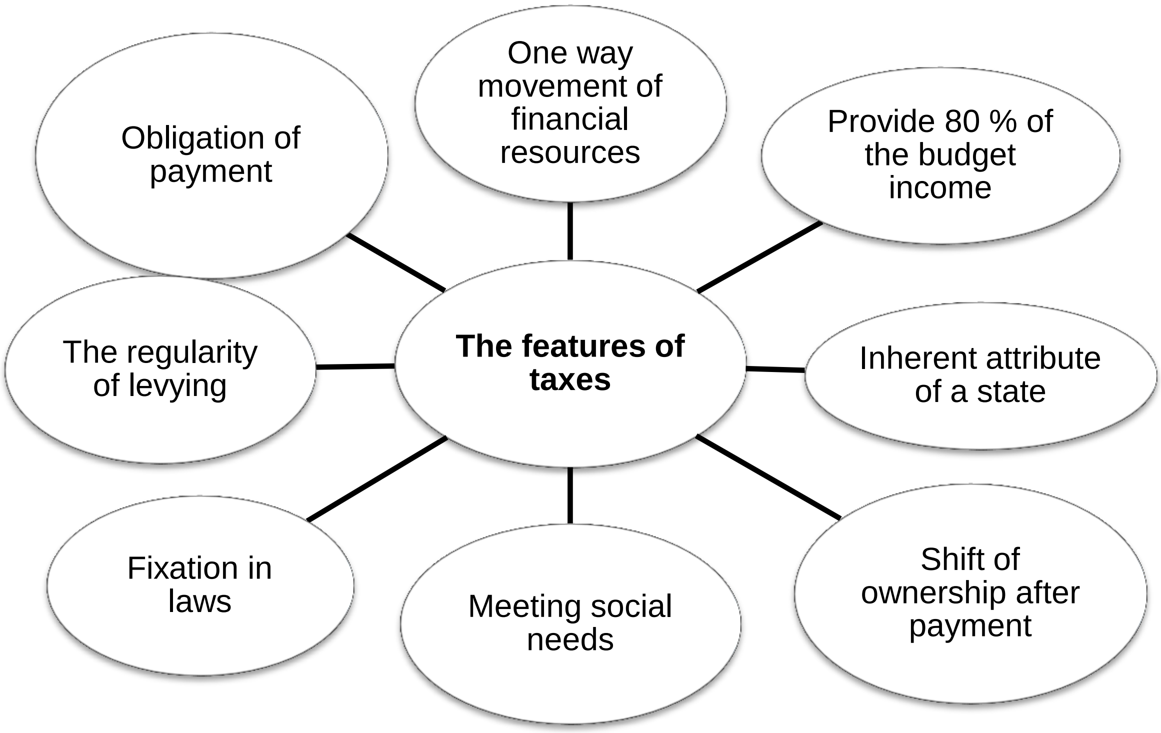

Fig. 4.1. **The features of taxes**

4.2. Taxation elements. Classification of taxes

Each tax can be characterized by a set of basic and additional elements. The basic ones are the subject (payer) of the tax; the object of the tax; the rate of the tax. The additional elements include the tax base, the taxation unit, the source of the tax (fee) payment, the tax statement, the tax benefit, the tax quota.

Classification of taxes is given in Table 4.1.

Table 4.1

Classification of taxes

Criterion	Type of tax
State bodies which set a tax	State taxes
	Local taxes and fees
The source of payment	Taxes, fees and obligatory payments which are included in total expenditures and costs of production
	Taxes, fees and obligatory payments which are paid from enterprises profit or capital
	Taxes and fees which are included in the price of goods
The economic feature of the taxation object	Taxes on incomes and profit
	Taxes on consumption
	Taxes on property
The way of levying	Direct taxes
	Indirect taxes
The taxation subject	Taxes from legal entities
	Taxes from individuals
	Mixed taxes
The way of tax usage	General taxes
	Special (target)

4.3. The essence of the tax system and the principles of its construction

The tax system is a set of taxes in a country, which are interconnected, organically complementary, not in conflict with the whole system and its elements [16]. The structure of the Ukrainian tax system is given in Fig. 4.2.

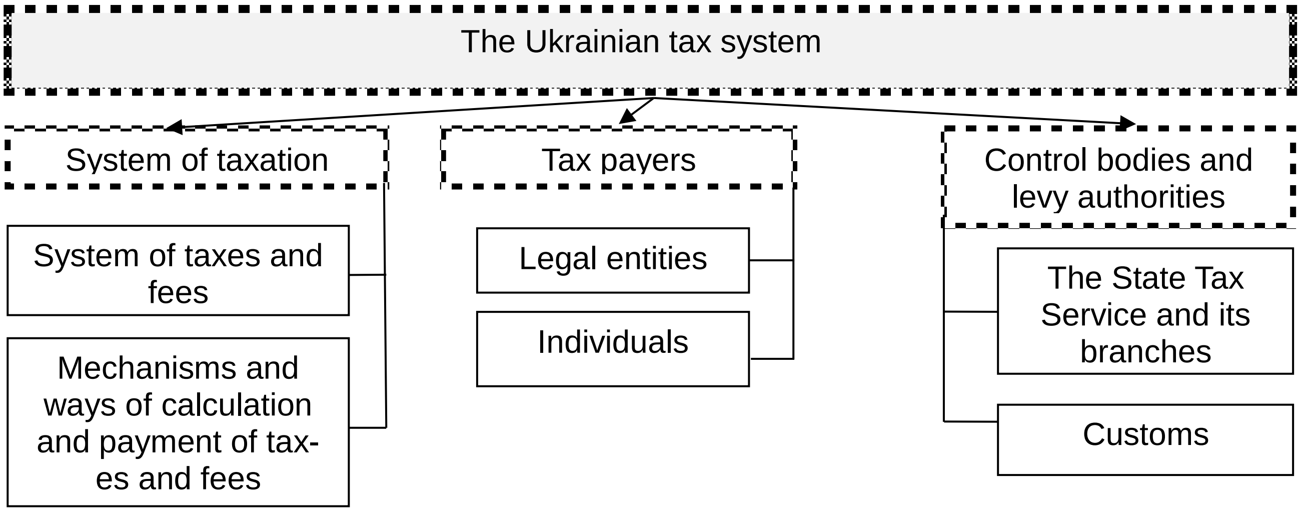

Fig. 4.2. **The structure of the Ukrainian tax system**

General taxes and fees in Ukraine are: the tax on enterprises' profit; the tax on individuals incomes; the value added tax (VAT); the excise tax; the fee for the first registration of a vehicle; the environmental tax; the rent for transportation of crude oil and petroleum products by main pipelines, transit transportation of natural gas and ammonia across the territory of Ukraine; the fee for subsoil use; payment for land; the fee for the use of the radio frequency resource of Ukraine; the fee for special use of water; the fee for special use of forest resources; the fixed agricultural tax; the fee for the development of viticulture, horticulture and hop; the fee in the form of a target premium to the current tariff for electricity and heat energy; the fee in the form of a target premium to the current tariff on natural gas for consumers of all forms of ownership.

Local taxes are: the tax on estate property apart from a land plot; the single (flat) tax. *Local fees are:* the fee for certain types of entrepreneurial activity; the fee for parking; the touristic fee.

The conditions and key components of the biggest state taxes in Ukraine are given in Fig. 4.2 – 4.5.

Taxation base	Monetary form of legal entities' profit
Tax payers	Legal entities which conduct business activity in the territory of Ukraine and abroad
Tax rate	From 1.04.2011 to 31.12.2011 – 23 %. From 1.01.2012 to 31.12.2012 – 21 %. From 1.01.2013 to 31.12.2013 – 19 %. From 1.01.2014 to 1.12.2014 – 18 %. From 1.01.2015 to 1.12.2015 – 17%. From 1.01.2016 – 16%
Terms of payment	Tax declaration is prepared and submitted once a year
Fine for schedule disruption	The fine is charged at the rate of 120 % per annum of the NBU discount rate per each day of delay

Fig. 4.2. **The tax on enterprises' profit**

Base taxation	Income paid (provided) in favor of a taxpayer during the reporting tax period
Tax rate	18 %
Tax payers	Physical person – resident who derives income from a source of origin in Ukraine and foreign incomes
Tax terms	Shall be paid (transferred) to the budget during the payment of taxable income
Fines for disruption	Charged at the rate of 120 % per annum of the NBU discount rate per each day of delay

Fig. 4.3. **The tax on individuals' income**

Taxation base	The cost of goods and services delivered in the customs territory of Ukraine
Tax rate	From 1 January 2015 – 17 % (planned), in fact – 20 %. 7 % – applies to the operations defined in the Article 193 of the TC. 0 % – applies to the operations defined in the Article 195 of the TC
Tax payers	The tax is paid directly by byers, but the process of its withholding and payment to the budget is carried out by the seller
Tax terms	A declaration has to be submitted monthly or quarterly in electronic form
Fine for disruption	Charged at the rate of 120 % per annum of the NBU discount rate per each day of delay

Fig. 4.4. **The value added tax**

Taxation base	Excisable goods: alcohol ethyl and other spirit distillates, alcoholic drinks, beer; tobacco and manufactured tobacco substitutes; petroleum products, liquefied gas; motor vehicles, bodywork, trailers and semi-trailers, motorcycles
Tax rate	Tax rates are set by Art. 215 of the Tax Code and are uniform throughout the territory of Ukraine: ad valorem, specific, ad valorem and specific at the same time
Tax players	1. Legal entities and individuals who produce excisable goods (products) in the customs territory of Ukraine. 2. Business entities, individuals (residents or nonresidents), who import excisable goods (products) into the customs territory of Ukraine
Tax terms	Monthly
Fine for disruption	Charged at the rate of 120 % per annum of the NBU discount rate per each day of delay

Fig. 4.5. **The excise tax (fee)**

Questions for self-assessment

1. What is the difference between tax, fee and duty?
2. Name and explain the functions of taxes.
3. What features of a tax can be distinguished?
4. What elements should any tax be characterized with?
5. What types of taxes exist in the world practice?
6. Identify the general taxes and fees in Ukraine.
7. Explain the features of the enterprises' profit tax.
8. Explain the features of the individual income tax.
9. Explain the features of the excise tax.
10. Explain the features of the value added tax.

Practical tasks

Task 1. Define the volume of the value added tax (VAT) which must be paid to the state budget (or returned from the budget) based on the results of the current period.

The output data

The cost of goods and operations performed during a month:

1. Goods sold in the territory of Ukraine – 60 000 UAH (without VAT).
2. Stationery bought from a domestic manufacturer – 2 400 UAH (with VAT).
3. Pecuniary aid (subsidy) provided to a local hospital – 1 700 UAH.
4. Goods exported – 180 000 UAH.
5. Materials for production received from suppliers – 35 000 UAH (without VAT).
6. The cost of goods bought for a company which will be included to the total cost of production – 42 000 UAH (with VAT).
7. A workshop given to financial leasing – 6 000 UAH (with VAT).

Task 2. A company has shown the following indicators during the current period (Table 4.2).

Table 4.2

Name of goods	Output, items	Sold items	Cost per item, with VAT, UAH
A	1400	1380	48
B	3000	2990	62
C	1100	1059	36

To produce these goods the company bought raw materials – 92 640 UAH (with VAT) which are used in production. Using the given data, define:

a) tax liability;

b) tax credit;

c) the amount of the VAT which must be paid to the budget.

Task 3. Define the level of income which makes it possible to receive a social tax benefit based on the subsistence level for an able-bodied person in Ukraine for the period from 2011 to 2017 (Table 4.3).

Table 4.3

Period	Subsistence level
01.01.2017	1600
01.09.2015	1378
01.01.2015	1218
01.01.2014	1218
01.01.2013	1147
01.01.2012	1073
01.01.2011	941

Task 4. Calculate the individual income tax for an employee of the Omega company for January 2017 using the company's staff list (Table 4.4).

Table 4.4

Company's staffing

No.	Name	Position	Salary per month, UAH
1	R. Potepov	Deputy director	14 000
2	O. Homenko	Chief accountant	9 567
3	S. Kvitka	Sales manager	4 567
4	T. Soshko	HR manager	3789
5	O. Onopko	Watchman	900

Methodical recommendations

The equations for calculating the individual income tax IIT are as follows:

1. If an employee doesn't have the right to a social tax benefit:

$$\textit{Individual income tax} = \textit{salary} \times 18\ \%. \qquad (4.1)$$

2. If an employee has the right to a social tax benefit (STB):

$$\textit{Individuals income tax} = (\textit{salary} - \textit{STB}) \times 18\ \%. \qquad (4.2)$$

The volume of the social tax benefit in 2017 is given in Table 4.5.

Table 4.5

The volume of the social tax benefit in 2017

The maximum amount of income that gives the right to tax benefits, UAH	Subsistence level (SL), UAH	The volume of STB, 50 % of SL, UAH	The size of STB, UAH		
			100 % of STB	150 % of STB	200 % of STB
2240.0	1600.0	800.0	800.0	1200.0	1600.0

Social tax benefit can be applied to an income per month if its volume doesn't exceed the figure received as a multiplication of the current subsistence level and the coefficient 1.4.

Task 5. Define the profit tax of the PJSC "Svitanok" (dairy product manufacturer) for March 2015 if the following business operations were conducted:

• 3 March – milk was bought from the "Ferma Ltd" company for cheese manufacturing – 5 800 UAH (without VAT);

• 4 March – prepayment from the PC "Class" was received for a cheese consignment for sale in April – 7 250 UAH (with VAT)

• 15 March – cheese was sold to the PC "Furshet". Revenue from sale amounts to 36 500 UAH (with VAT);

• salary and wages of employees engaged in production amount to 14 200 UAH;

• overheads on cheese production – 834 UAH;

• costs of sales – 215 UAH;

• depreciation of assets – 427 UAH;

• 23 March – PJSC "Svitanok" paid debt recovery of 7 420 UAH.

Methodical recommendations

Incomes include: revenue from sales of goods and services, dividends, operational leasing, fines on court decision, the cost of free goods and services received by a company, revenue from sales of non-current and current assets, etc. *Incomes do not include:* prepayments, the amount of the VAT, money or cost of property received as direct investments or reinvestments in corporate rights, overpaid tax returned from the budget, income from security issuance, the sum of credits and loans.

Expenditures include: cost of production of goods and services (material costs, wages, depreciation, overheads, etc.); other expenditures (administrative costs, costs of sales, financial costs, etc.). *Expenditures do not include:* costs of meetings, presentations, events, entertainment; prepayments; repayment of the sum of credits and loans; cost on non-current assets buying or building; dividends; the cost of trade patents, etc.

Topic 5. Budget. The budgetary system

The aim is to form theoretical knowledge as for the nature of budget, budgetary relations and budgetary system functioning; to develop the ability to assess the effectiveness of the state budgetary system, to define the rate of debt security.

The main issues

5.1. Budget as an economic category.

5.2. Budget as a schedule of income and expenses.

5.3. The formation and development of the budgetary system in Ukraine. The nature and methods of the budgetary policy formation.

The competences to be formed:

knowledge:

the nature of budget and budgetary system;

the levels of the budgetary system in Ukraine;

the structure of the consolidated budget of Ukraine;

skills:

to define the bases of budgeting;

to determine the levels of the budgetary system in Ukraine;

to analyze the main indicators of the budget, which form its balance;

communication:

the ability to identify the core elements of the budget of Ukraine;

the ability to implement the basic principles of the budgetary system functioning;

autonomy and responsibility:

the definition of the features of the Ukrainian budgetary system functioning and budgetary process at both the general and local levels;

the analysis of the resources of the consolidated budget.

Key words: state budget, consolidated budget, income (expenses) of budget, budgetary relationships, budgetary system, process of budgeting, local budget, budgetary policy, budgetary tactics, budgetary strategy.

5.1. Budget as an economic category

As an economic category, *the state budget* reflects the financial relations associated with the formation and use of state funds [24].

Budgetary relations cover the basic elements of the total social product cost and the various ways of its usage.

The state budget is a combination of legally regulated relations between the state, legal entities and individuals concerning the distribution and redistribution of the GDP for the purpose of centralized fund formation and use, designed to ensure the implementation of state functions.

The interpretation of the concept of budget is given in Fig. 5.1.

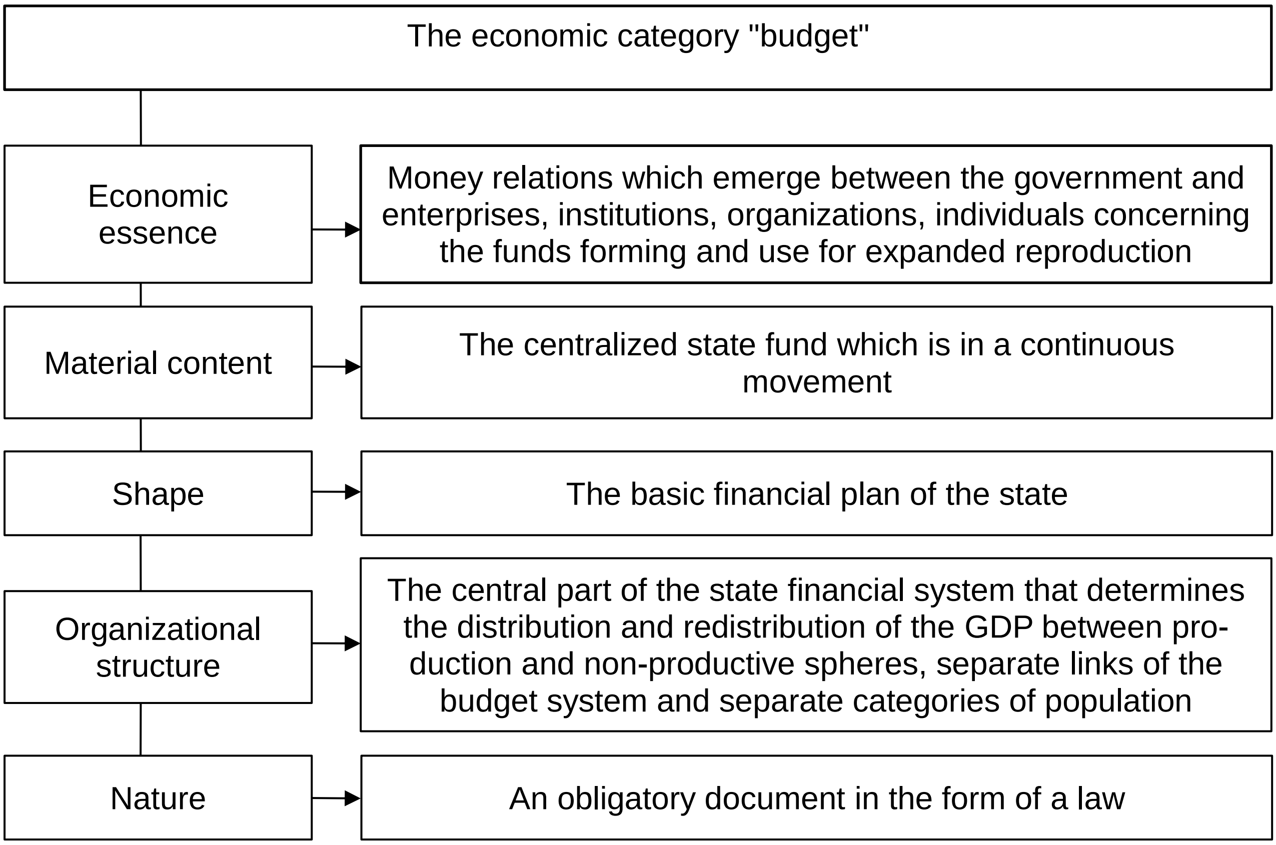

Fig. 5.1. **The interpretation of the concept of budget**

The signs of budgetary relations are:

redistributive character – budget realizes the functions of redistribution of the GDP between the sectors, regions, segments of population;

comprehensive nature – covering all the individuals and legal entities;

being regulated by the law – regulated by the Budget Code; by the laws about the flow of revenues and cost financing; by the annual law about the budget for the current year [21].

Budgetary relations are a part of financial relations. Budgetary relations form the budgetary policy of the state (not conversely).

The functions of a budget are the following:

the distributive function (the state concentrates all the sources of budget revenues and distributes them vertically (between the ministries, departments, top managers of budgetary funds) and horizontally (between different sectors, territories));

the control function (special state or public authorities control the accumulation of budget funds (budget revenues), their distribution (budget expenses) and align the budget);

the function of the state existence provision (the creation of a financial base for the state existence, for the presidential, legislative and executive authorities, law enforcement and customs authorities, tax service, the implementation of international economic activity);

the incentive function (provides just distribution of state funds between business entities for the purpose of their economic activity stimulation and revitalization).

Budgetary organization is the organization and principles of the budgetary system construction, its structure, distribution of income and expenditure between separate links, the legal basis of budget functioning, the formation of the relationship between the budgets and the relation between the parts of the budget system.

There are 3 ways to form budget:

to form a single budget for the whole country;

to form separate regional budgets;

to form centralized and decentralized types of budgets at every level of administrative division.

The central budget in Ukraine is the *State Budget.* The *local budget* depends on the level of administrative division and is divided into:

centralized, according to the administrative units (regional, area, city).

decentralized (city, village, district in cities).

5.2. Budget as a schedule of income and expenses

The schedule is the document that establishes the distribution of income and the budget expenses financing between the main managers of budgetary funds for certain periods of a year according to the budget classification [21].

Budget income (revenue) is a part of the state centralized financial resources which are regulated by the relevant rules and necessary to perform its functions (Table 5.1). The revenues reflect the economic relationship between the government and enterprises, institutions, organizations, and individuals that emerge in the process of collecting budget payments [21].

Budget expenses (expenditures) are the government expenditures at the state level which are necessary for the state to fulfil its functions. These costs express the economic relations as the base of the central funds use according to a certain law.

Table 5.1

Classification of the state budget incomes

Type	Characteristic
1	2
The source of formation	The revenues received from the distribution of additional value – national income (NI)
	Revenues, which are a part of the fund (the share of depreciation)
	Income from the sale of national wealth
The socio-economic signs	Income from economic (business) activity
	Income from the use of natural resources
	Revenues from international activity
	The income from banking activities
	Revenues from the sale of precious metals from the State Fund of Precious Metals and Precious Stones
	Tax revenues
	State fee
	Other tax revenues
	Non-tax revenues
	Privatization revenues

Table 5.1 (the end)

1	2
The sections according to the budget classification	Tax revenues (taxes, fees and obligatory payments)
	Non-tax revenues (revenues from property and entrepreneurial activities, income from fines, etc.)
	Revenues from capital transactions (from the sale of abandoned property, property that became the state ownership, and treasure)
	Official transfers (subsidies, grants)
	Target funds

A budget consists of three parts: general, special and reserve funds.

The general fund is made up of:

1) all revenues, except for those that are intended to be enrolled to the special fund of the budget;

2) all the budget expenses provided by the general fund income;

3) lending of the budget (the return of credits to the budget without identifying the target areas and the loans providing from the budget, that is realized with the general fund income.

The special fund is made up of:

1) budget revenues (including the revenues of budgetary institutions) that have a target direction;

2) expenditures which are financed from the budget special fund in the form of specified revenue (including the revenues of budgetary institutions);

3) lending of the budget (the return of credits to the budget with the definition of target areas and the provision of loans from the budget provided by the specified revenue of the special fund).

The reserve fund is designed to provide emergency expenses for activities that could not be predicted during the budget approval or due to extraordinary circumstances.

5.3. The formation and development of the budgetary system in Ukraine. The nature and methods of the budgetary policy formation

The legislative and regulatory basis for the Ukrainian budgetary system functioning is shown in Fig. 5.2.

The budgetary policy is a set of measures for attracting, distribution and use of funds of the state budget [5].

The budgetary forecasting is the process of development of the state budget key indicators for the future, prediction of the most important revenues and expenditures. During this process the concept, the main purpose, the main development directions and aims are determined and must be achieved.

Fig. 5.2. **The legislative basis for the Ukrainian budgetary system**

The budgetary planning is a scientifically-based process aiming to identify the sources of budgetary resources creation and use to ensure the ongoing economic and social development.

Questions for self-assessment

1. Give a definition of the state budget as an economic category.
2. Name and explain the signs of budgetary relations.
3. Name the functions of the budget.
4. Give a definition of budgetary organization.
5. What factors influence the budget of a state?
6. Explain the structure of the budget, budget incomes and expenditures.

7. How can the state income be formed?

8. Explain the legislative and regulatory basis of the Ukrainian budgetary system functioning.

Practical tasks

Task 1. Define the total amount of budget expenditures and budget financing using information from Table 5.2.

Table 5.2

Initial information for doing the task

Indicators	The value of the indicator, million UAH
Credit provision from the budget	10.2
Return of credits to the budget	8.4
Internal loans	63.7
Repayment of internal liabilities	22.3
Repayment of external liabilities	19.8
Placement of budget funds on deposits	6.7
Purchasing securities	3.4
Return of budget funds from deposits	2.6
Income resulting from selling / presenting securities	4.7
Budget expenses	380.5

Methodical recommendations

According to the Budget Code of Ukraine (Art. 2), *budget expenditures* include budget expenses, credits provision from the budget, repayment of loans, placement of budget funds on deposits and purchasing securities.

Having chosen components from the list and having found their sum you will get the total amount of budget expenditures.

Budget financing (according to Art. 2 of the Budget Code) includes: incomes and expenditures of the budget which are related to the change of the debt volume, volumes of deposits and securities; funds from privatization;

change of remains of budget funds used to cover the budget deficit or define the budget surplus. Thus, the volume of budget financing is calculated as a sum of the following components:

1) financing debt operations as a difference between the amount of granted and repaid loans (internal and external);

2) funds from privatization;

3) financing active operations: the difference between incomes from selling/presenting securities and the cost of purchased securities; the difference between the volume of returned budget funds from deposits and the sum of budget funds placed on deposits; changes of budget funds, namely: runup/reduction of remains on the reported period; increase or devaluation of UAH as a result of differences in exchange; internal transference of funds (between funds); financing from the single Treasury account, etc.

Having chosen these components from the list and having summarized them you will get the volume of budget financing.

Task 2. Fill in the gaps in Table 5.3 and define the budget incomes.

Table 5.3

The dynamic indicators of the budget incomes

Year	State incomes, million UAH	Dynamic indicators			
		runup	rate of growth, %	rate of runup, %	The value of 1 % of runup
2010	20689.9	-	-	-	-
2011	…	…	146.1	…	…
2012	…	…	…	2.86	…
2013	…	3960.4	…	…	…
2014	…	…	…	49.4	…

Topic 6. The essence, principles and role of insurance

The aim is to create a comprehensive understanding of the economic essence of insurance and its role in economy, to gain a theoretical understanding of the basic functions and principles of insurance, types of insurance according to various classification criteria, as well as the essence of voluntary and obligatory forms of insurance.

The main issues

6.1. The essence of insurance as an economic category.

6.2. The functions and principles of insurance.

6.3. Classification of insurance. Forms of insurance: obligatory and voluntary.

The competences to be formed:

knowledge:

the economic essence of insurance, its functions and principles;

types of insurance according to various classification criteria;

skills:

to analyze the organization of insurance provision;

to identify advantages and disadvantages of voluntary and obligatory forms of insurance;

communications:

the ability to define the functions and principles of various forms of insurance;

the ability to provide the insurance process;

autonomy and responsibility:

to evaluate the advantages of insurance over self-insurance;

to determine the peculiarities of compensations for double insurance.

Key words: insurance, insurance market, insurance case, policyholder, insurer, insured, insurant, insurance risk, insurance fee, insurance payment, insurance premium, insurance compensation, insurance amount, insurance rate, voluntary insurance, obligatory insurance.

6.1. The essence of insurance as an economic category

The origin of the word "insurance" comes from the old expression "to act at one's own risk", i.e. on one's own responsibility.

To prevent losses from hazardous events, humanity has developed two main ways of protecting their interests – *preventive and repressive*.

The first method provides prevention of such events through construction of modern buildings resistant to fire and the establishment of reserves for the emergency period.

The second way implies the suppression and elimination of consequences of the coming dangerous, adverse events, such as fire fighting, construction of dams and organization of the evacuation of people from flood zones.

Insurance is protection against the effects of dangerous, adverse events, not all, but only random ones, which may come with the probability that it is not possible to know in advance where exactly, when and who they may happen to.

Such events could be a hurricane destroying homes in its path, fire in the house, an accident on the road, etc. The possibility that such events will occur is called a risk. The man who owns a house and a car, knows that an adverse set of circumstances that will lead to a fire or accident is possible, but has no idea when it can happen.

A random event is an alleged event that could happen (occur). If it happens, it is called an insurance case.

Probability is a numerical measure of the degree of objective possibility of an event.

An insurance case, in fact, is a random event happened in the aftermath of which, under the insurance contract, the insurer is obliged to recover damages or to pay the insured amount.

The insurance amount is a sum of money set by the law or the insurance money at which the insurer valued his property interests at risk.

Insurance is one of the oldest and most sustainable forms of financial and economic life, rooted in the distant history. The objective need for insurance at all times is driven by the fact that the damage arising from sudden, accidental destructive factors beyond a person (natural forces of nature, hostilities, civil disturbances, accidents), disasters, criminal acts (theft, robbery), his own negligence, could not always be recovered from the perpetrator, and leads to the loss and devastation of victims. Only a pre-established special insurance fund could be the source of recovery of damages.

In general, the economic essence of insurance is characterized by the following signs: the existence of redistribution; availability of insurance risk and criteria for its evaluation; formation of the insurance community of insured persons and insurers; a combination of individual and group insurance interests; joint and individual liability of all insurers for the damage; a closed-circuit mode of damage; redistribution of damage in time and space; repayment of insurance premiums (distributed in space and time); self-insurance activities.

The specificity of insurance as an economic category is defined by the following features: random nature of natural disaster or other circumstances of climatic, economic and social nature; expression of damages in kind or value (cash); uneven damage to different entities; an objective need for reimbursement of damage; taking measures for preventing and overcoming the consequences of the event.

According to the Law of Ukraine "On Insurance", *insurance* is a type of civil law relations on protection of property interests of individuals and legal entities in case of occurrence of certain events (insurance cases) identified by the insurance contract or applicable law, at the expense of funds that are generated through the insurance payments (insurance contributions, insurance premiums) paid by individuals and legal entities and income from investment of these funds.

The insurer is a legal entity in the form of joint stock, full or limited partnerships or companies with additional liability established to conduct insurance business and have an appropriate license.

Policyholders (insurants) are legal entities and capable individuals who entered into the contract with insurers or who are insured according to the legislation of Ukraine.

The insurance market is considered as a system of economic relations which defines formation of supply and demand for insurance products; the object of buying – selling is insurance protection as a form of communication between the participants in insurance legal relations.

Depending on the demand and supply scale for insurance services, internal (regional), external and international insurance markets can be distinguished. The internal (regional) insurance market is the local market where there is a direct demand for insurance services. *The external insurance market* is the market which goes beyond the domestic market. *The world (international) insurance market* is connected with supply and demand for insurance services in the scale of the world economy.

A specific product offered in the insurance market is *insurance service*. Its utility value is the *provision of insurance protection*. The price of insurance services is expressed in the *insurance tariff (rate).* It is formed on a competitive basis, comparing demand and supply.

The actors in the insurance market are given in Fig. 6.1.

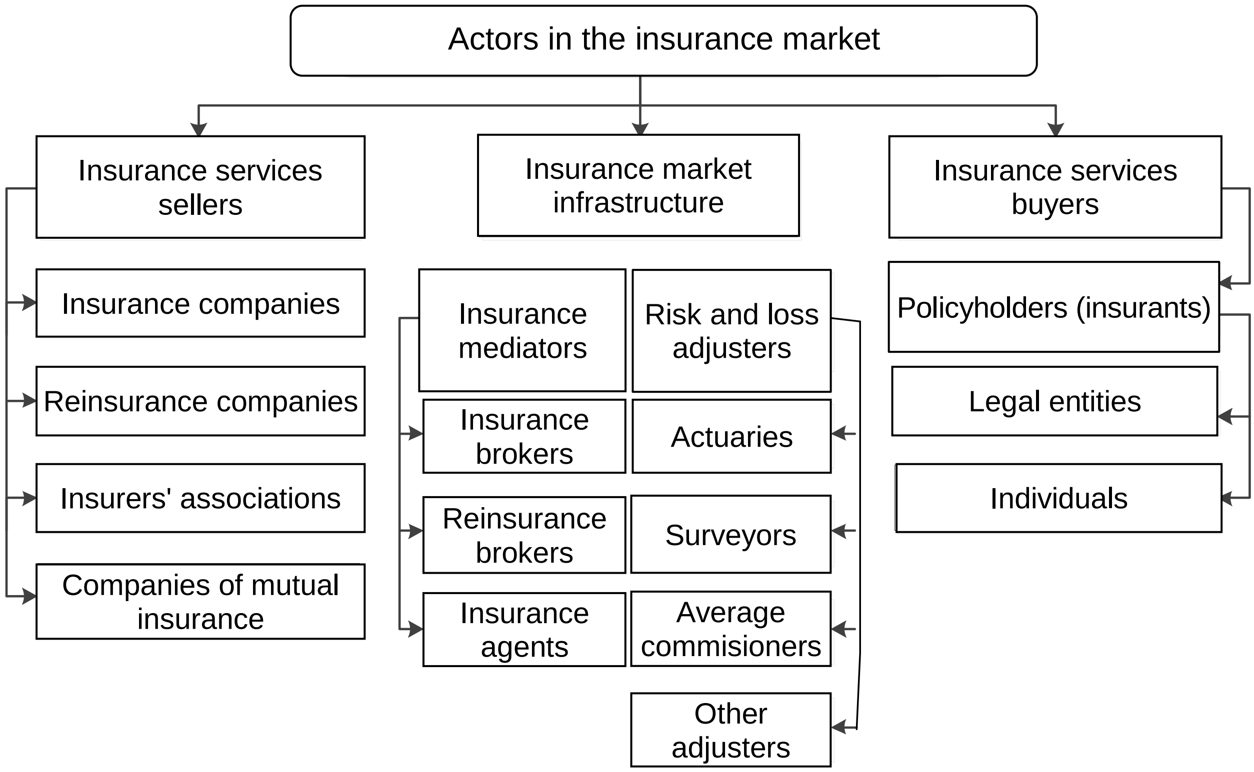

Fig. 6.1. **The actors in the insurance market**

The insurer is an organization which, in accordance with the received license, undertakes, for a certain fee, an obligation to compensate damage to a policyholder or persons whom he named, or to repay the insured amount if the insurance event occurs.

The insurance company is a legal unit of business which takes the obligations of the insurer and has an appropriate license.

Insurers can form unions, associations in order to coordinate their activities, protection of its members' interests and implement joint programs if their setting up does not contradict the legislation of Ukraine.

According to the legislation of Ukraine, the following insurance unions can act: the Bureau of Aviation Insurance, the Marine Insurance Bureau, the Nuclear Insurance Pool, the Agricultural Insurance Pool, the Motor (transport) Insurance Bureau of Ukraine.

Individuals and legal entities can create mutual insurance companies for the purpose of insurance protection of their property interests. A mutual insurance society is a nonprofit organization created for the purpose of providing insurance protection of property interests of its members.

Policyholders are individuals and legal entities who have decided to enter into an insurance contract with any seller.

Insurance brokers are legal entities or individuals registered as subjects of entrepreneurial activity and conducting intermediary activity in insurance for remuneration on their behalf on the basis of a brokerage agreement with a person who has a need for insurance as a policyholder.

Reinsurance brokers are legal entities who carry out intermediary activity in reinsurance for remuneration on their behalf on the basis of a brokerage agreement with an insurer who has the need for reinsurance as a reinsurer.

Insurance agents are individuals or legal entities that act on behalf of the insurer and perform part of its insurance activity, namely: conclude insurance contracts, receive insurance payments, perform work associated with the implementation of insurance payments and insurance claims.

Insurance agents are representatives of the insurer acting on their behalf for remuneration according to the Contract of the Agency.

A surveyor is an inspector or agent of the insurer who inspects property accepted on insurance. Based on the conclusion of the surveyor, the insurer decides whether to enter the insurance contract or not.

In case of the insured event, the determination of the causes, nature and scale of losses caused by this event is the duty of the *average commissioner*. The conclusion of the average commissioner is applied to the insurer and leads to acceptation or rejection of the insurant's claim.

The average commissioner in marine insurance is the *adjuster*. His responsibilities include the distribution of losses between the parties (ship, freight and cargo).

An actuary is a specialist on risk assessment, a financial analyst or a consultant in the insurance industry. It is an officially authorized person who has professional training and calculates insurance rates. The actuary has a responsibility for the insurance funds sufficient at the time when the insurer has to comply with their obligations under insurance contracts.

6.2. The functions and principles of insurance

Primary functions:

Providing certainty. Insurance provides certainty of payment at the uncertainty of loss. The uncertainty of loss can be reduced by better planning and administration. There is uncertainty of happening of time and amount of loss. Insurance removes all these uncertainties and gives certainty of payment of loss. The insurer charges premium for providing such certainty.

Providing protection. The main function of insurance is to provide protection against the probable chances of loss. The time and amount of loss are uncertain and in case of happening of risk, the person will suffer from loss in the absence of insurance. Insurance guarantees the payment of loss and thus protects the insurant from sufferings. Insurance cannot avoid the accident but can provide compensation for losses in case of happening of risk.

Risk-sharing. The risk is uncertain, and therefore, the loss arising from the risk is also uncertain. When risk takes place, the loss is shared by all the persons who are exposed to the risk. In the ancient time risk sharing was done only at the time of damage or death, but today, on the basis of probability of risk, the share is obtained from each and every insured in the form of premium without which protection is not guaranteed by the insurer.

Secondary functions:

Prevention of loss. The insurance joins hands with those institutions which are engaged in preventing the losses of the assured and so more saving is possible which will assist in reducing the premium. Lesser premium invites more business and more business causes lesser share to the assured. So again premium is reduced, which will stimulate more business and more protection to the masses. Therefore, the insurance assists financially in the activity of health organizations, fire brigades, educational institutions and other organizations which are engaged in preventing the losses of the masses from death or damage.

Providing capital. Insurance provides capital to society. The accumulated funds are invested in a productive channel. The industry, the business and the individual benefit from the investment and loans of the insurers.

Improving efficiency. Insurance eliminates worries and miseries of losses in the case of death and destruction of property.

Assisting in economic progress. Insurance protects society from huge losses of damage, destruction and death, provides an initiative to work hard for the betterment of the masses. The next factor of economic progress, the capital, is also immensely provided by the masses. The property, the valuable assets, the man, the machine and the society cannot lose much in the case of disaster.

The basic principles of insurance are the following: the principle of free choice of the insurer; competitiveness; the principle of trust; insurable interest; the principle of causation; compensation of losses; franchise; subrogation; contribution; diversification; coinsurance and reinsurance.

6.3. Classification of insurance. Forms of insurance: obligatory and voluntary

Classification of insurance is given in Fig. 6.2.

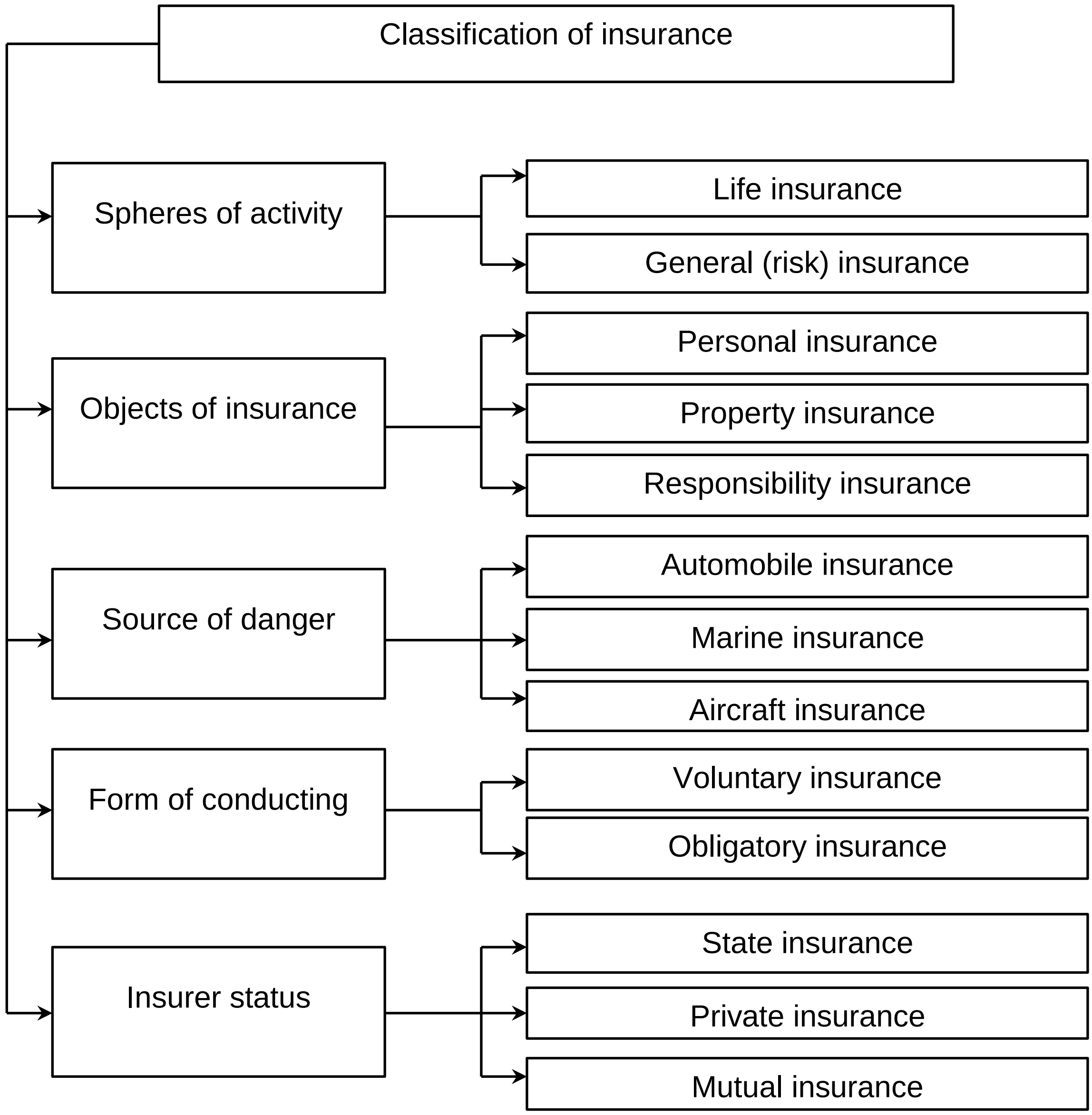

Fig. 6.2. **Classification of insurance**

Obligatory insurance is divided into the following types (according to the law "On Insurance"):

1) medical insurance;

2) personal insurance of medical and pharmaceutical workers in case of infection with human immunodeficiency virus in the course of performance of their official duties;

3) personal insurance of workers of departmental fire protection and members of voluntary fire teams (except those who work at institutions and organizations that are financed from the state budget of Ukraine);

4) insurance of athletes of higher categories;

5) life and health insurance of specialists of veterinary medicine;

6) personal insurance against accidents on transport;

7) aviation insurance of civil aviation;

8) insurance of civil liability of vehicle owners;

9) insurance of water transport;

10) insurance of civil liability of the operator of a nuclear unit for nuclear damage which may be caused as a result of a nuclear incident;

11) insurance of employees that take part in provision of psychiatric care (except those working at institutions and organizations that are financed from the state budget of Ukraine);

12) insurance of civil liability of business entities for damages that may be caused by fires and accidents at high risk objects, including fire and explosion hazard objects and objects of economic activity which can lead to accidents of ecological and epidemiological nature;

13) insurance of civil liability of the investor, including that for damage caused to the environment, human health, according to the agreement on product distribution, unless otherwise provided in the agreement;

14) insurance of property risks of industrial development of oil and gas fields in cases stipulated by the Law of Ukraine "On Oil and Gas";

15) insurance of medical and other workers of state health care scientific institutions (except those working at institutions and organizations that are financed from the state budget of Ukraine) in the case of infectious diseases associated with performing professional duties;

16) insurance of responsibility of the exporter and the person responsible for utilization (removal) of hazardous wastes, concerning compensation of damages that may be caused to human health, property;

17) insurance of objects of space-based activity;

18) insurance of liability of dog owners (for the list of breeds identified by the Cabinet of Ministers of Ukraine) as for the harm that may be caused to third parties;

19) insurance of animals (except those used for agricultural production) in case of death, destruction, illnesses;

20) insurance of responsibility of companies providing tourist services for damage to life or health of the tourist or his property;

21) liability insurance of a marine owner and so on.

Questions for self-assessment

1. Give a definition of the concept "insurance".
2. Name the principles of insurance.
3. Name and explain the primary functions of insurance.
4. Who can be an insurer in our country?
5. What are the peculiarities of the insurance market?
6. What is the difference between the actuary and the adjuster?
7. What types of insurance belong to the obligatory insurance?
8. Name five most popular types of insurance in Ukraine.

Practical tasks

Task 1. The insurance amount is 2 500 UAH, the conditional franchise is 20 % of the insurance amount. The amount of losses is 450 UAH. Define the size of the insurance compensation.

Task 2. The insurance amount is 5 100 UAH, the unconditional franchise is 20 % of the insurance amount. The amount of losses is 1 200 UAH. Define the size of the insurance compensation.

Task 3. The property insurance contract between an insurer and a policyholder provides the use of franchise. The insurance amount is 500 000 UAH. The conditional franchise is 15 %. The amount of policyholder's losses as a result of the insured event amounts to 95 000 UAH. Define the size of the insurance compensation which must be paid to the policyholder in this case and if the losses amount to 60 000 UAH. Define the size of the insurance compensation if the franchise is unconditional.

Task 4. The car costs 90 000 UAH and it was insured for 80 % on the proportional liability system. As a result of the insured event, losses amount to 17 100 UAH. Define the size of the insurance compensation if according to the insurance contract the unconditional franchise is provided as 10 % of the insurance amount.

Task 5. A company entered into an insurance contract on profit loss insurance. The output data included profit of the previous year in the amount of 2 million UAH. Marginal responsibility of the insurance company is 80 %. Based on the results of the reporting period, the actual profit of the company is 1.5 million UAH. Define the size of the insurance compensation.

Topic 7. The financial market

The aim is to form a comprehensive understanding of relationships in the financial market; to get the basic principles of the financial market organization and functioning, the economic essence and usage of specific goods available in the financial market; to develop practical skills as for the evaluation of financial instruments.

The main issues

7.1. The essence of the financial market and its structure.

7.2. The subjects of the financial market.

7.3. The characteristics of the financial market objects.

7.4. State regulation of the financial market.

The competences to be formed:

knowledge:

the fundamentals of the financial market formation and functioning, the economic nature and structure of the financial market;

the basic principles and objectives of total product distribution through the mechanism of financial market;

skills:

to define prospects of the financial market development;

to evaluate the level of the financial market development and its structural elements;

to analyze and determine the priority directions of state regulation of the financial market;

communication:

the ability to determine the nature of the financial market as an element of the state financial system;

the ability to analyze the main factors that affect the structural elements of the financial market;

the ability to justify peculiarities of the financial market functioning and development in different countries;

autonomy and responsibility:

definition of peculiarities and priorities of the financial market development in Ukraine;

implementation of international best practices of the financial market functioning;

identification of negative factors influencing the financial market development in Ukraine.

Key words: financial market, financial resources, financial instruments (tools), money market, capital market, financial mediators, investors, borrowers, securities, financial services.

7.1. The essence of the financial market and its structure

The financial market is a combination of economic and legal relations arising between the participants and associated with the movement of financial resources necessary for the implementation of economic and financial activity; a set of economic relations concerning redistribution of temporarily free financial resources among the population, economic entities and the state through the system of financial institutions on the basis of supply and demand interaction [43].

The financial market exists as a set of interrelated and complementary markets. It is very important to associate the financial market with other markets, such as: the money market, the capital market, etc. The structure of the financial market is given in Fig. 7.1.

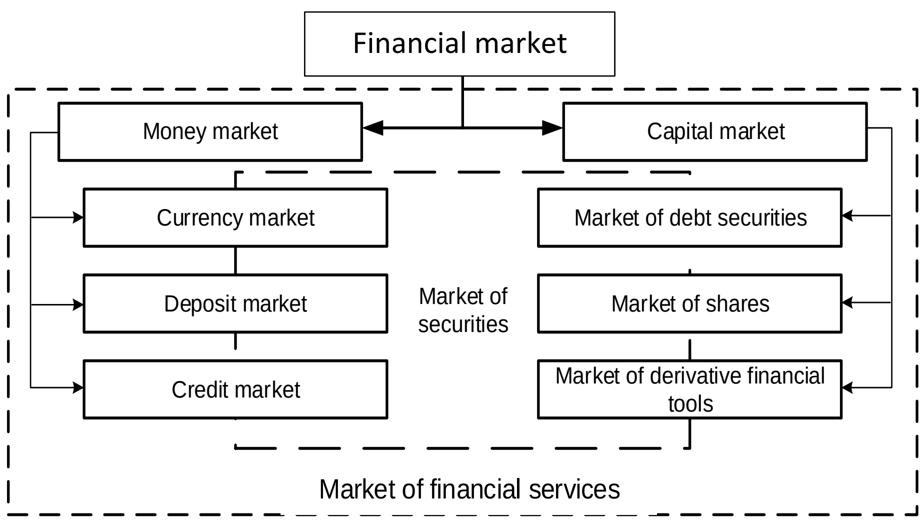

Fig. 7.1. **The structure of the financial market**

7.2. The subjects of the financial market

The financial market participants are the following:

Borrowers are individuals or legal entities lacking financial resources and attracting them to their development through financial instruments. Borrowers can be households, organizations, enterprises and the state when receiving credits and loans.

Investors are persons and entities that have surplus of financial resources and invest them in financial instruments.

Investors can be not only individuals and legal entities of Ukraine but foreign citizens and firms as well as the state, if they make a decision on money investment.

Mediators are financial institutions, providing interaction of the investor and the borrower. They can be bank institutions (investments, mortgages, savings, settlement banks) and non-bank institutions (insurance companies, out-state pension funds, institutions of join investments, credit unions, pawn shops, etc.) [43].

Other subjects of financial market are:

investment advisers (companies which provide services regarding transactions with financial instruments and financing);

subjects of the information infrastructure (financial media, specialized databases of certain types of financial assets and issuers, the state central fund of storage and information processing, information agencies);

subjects of the evaluation and analysis infrastructure (companies specializing in analytical information processing in financial markets; rating agencies which assess credit risk associated with securities; companies which evaluate the value of securities and other assets);

infrastructure subjects of the registrar (a registrar is an organization responsible for registration of security holders and transfer of ownership);

subjects of depositary, transfer agents, the clearing and accounting infrastructure (safekeeping of securities, collection, centralization and transmission of information on transactions registrars, specialized audit, etc.);

entities of the technological infrastructure (technological support and developing technologies that support financial markets, operations and infrastructure).

7.3. The characteristics of the financial market objects

The most widespread objects of the financial market are described in Fig. 7.2.

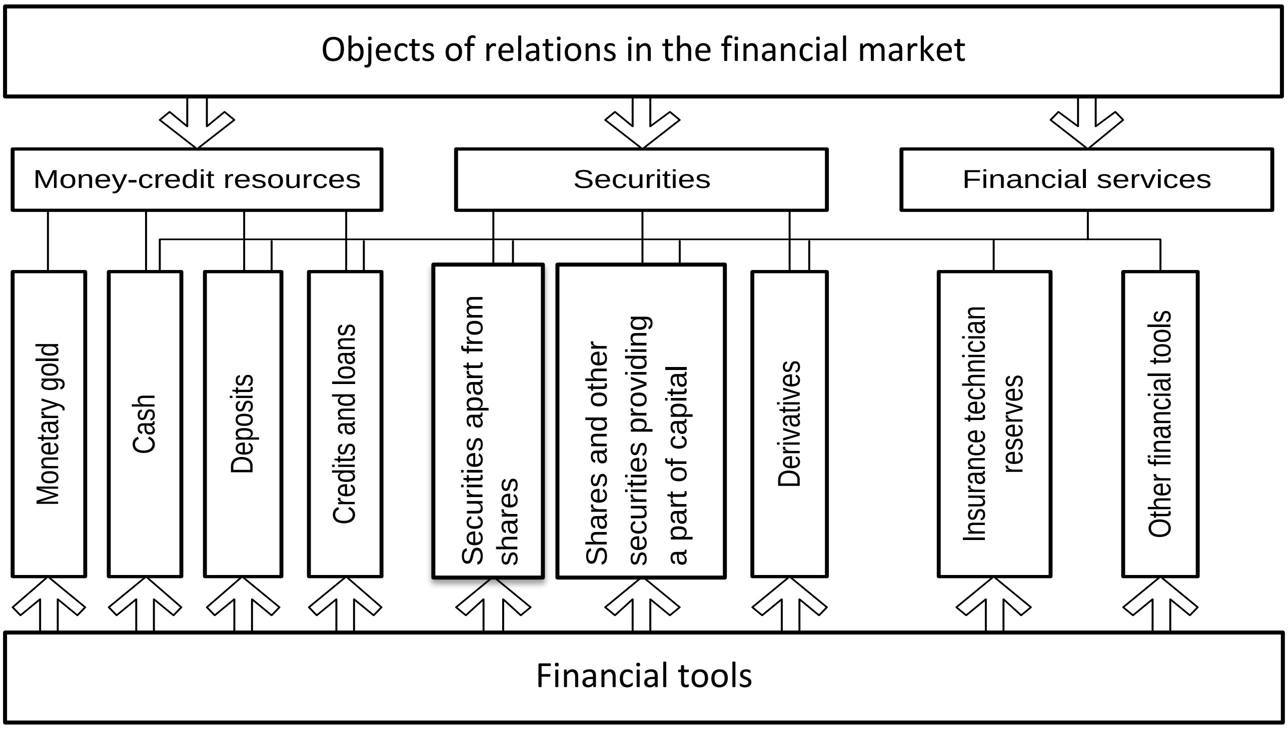

Fig. 7.2. **The objects of the financial market**

Debt securities are securities evidencing the loan relations and providing the obligation of the issuer to pay funds in the fixed term, to transfer goods or provide services in accordance with the obligation. They are the following: bonds of enterprises, bonds of local loans, treasury obligations of Ukraine, saving (deposit) certificates, state bonds of Ukraine, bills.

A bill is a request for payment of the money owed, or a piece of paper on which it is written [48].

A share is one of the equal parts that the ownership of a company is divided into, and that can be bought by public members [48].

A derivative is a financial product such as an option (the right to buy or sell something in the future) that has a value based on the value of another product, such as shares or bonds [48].

7.4. State regulation of the financial market

There are several basic models for financial market regulation. They can be distinguished according to three common criteria (Table 7.1).

Table 7.1

The regulative models of the financial market

Criterion	Model	Characteristic
Subject of regulation	Based on state regulation	A major role in regulation belongs in fact to the state authorities
	Mixed regulation	Regulation is divided between the state and self-regulatory organizations
Object of regulation	Functional	The object of regulation is the activity on the securities market, money market, credit market and so forth
	Institutional	The objects of regulation are financial institutions – banks, stock exchanges, insurance companies, etc.
	Mixed	A single mega-regulator of the financial market is created. The objects are financial conglomerates, which can include banking institutions and other non-bank financial institutions
Disclosure of information by market participants	State regulation	The legally set necessity for disclosure of information about the activities of the financial market participants
	Voluntary disclosure	Lack of regulatory requirements on information disclosure. Market participants voluntarily disclose economically feasible information

The system of the Ukrainian financial market regulation consists of three levels (the highest level is the level of legislative bodies; the middle one is the level of state regulative bodies; and the lowest level is the level of self-regulatory organizations (Fig. 7.3.) [28; 29].

The levels of the Ukrainian financial market regulation

I. The level of legislative bodies

Legislative activity of the Verkhovna Rada of Ukraine, the President of Ukraine, the Cabinet of Ministers of Ukraine

II. The level of state regulative bodies

Regulatory activity of the NBU, the National Commission on Securities and Stock Market, the National Commission on State Regulations of Financial Services Markets, etc.

III. The level of self regulatory organizations

Development and implementation of measures designed to protect the rights of members of self-regulatory organizations such as: the Association "Ukrainian Stock Traders", the Professional Association of Registrars and Depositories, the Ukrainian Association of the Investment Business, the League of Insurance Organizations of Ukraine, the National Association of Non-governmental Pension Funds of Ukraine and the Administrators of Non-state Pension Funds, the All-Ukrainian Association of Credit Unions, etc.

Fig. 7.3. **The levels of the Ukrainian financial market regulation**

The Ukrainian model of financial market regulation can be characterized by the following criteria.

1. Mixed regulation – regulation is divided between the state and self-regulatory organizations. The state administration belongs to the National Bank of Ukraine, the National Commission on Securities and Stock Market, the National Commission on State Regulation of Financial Services Markets, and the self-regulatory organization.

2. Functional (target) regulation – the objects of this regulation are:

activities in the market of securities and derivative financial instruments (the competence of the National Commission on Securities and Stock Market);

activities in the monetary market (the competence of the National Bank of Ukraine);

relations which occur between the participants in the financial services markets during the operations of financial services (the competence of the National Commission on State Regulation of Financial Services Markets).

3. Strict regulation is based on rigid, detailed rules, procedures and control of their appropriateness. The National Bank of Ukraine performs banking regulation and banking supervision. The National Commission on Securities and Stock Market deals with state regulation and control over the issuance and circulation of securities, their derivatives and the sphere of joint investments.

4. State regulation – legislative and normative documents are created to regulate the level of disclosure of information.

Questions for self-assessment

1. What is financial market?
2. What sense does financial market have for the state? For a company?
3. Who can be participants in the financial market?
4. What is the difference between shares and bonds?
5. What kinds of financial tools do you know?
6. How can the activity in the financial market be regulated? Who is the biggest regulator?
7. What is the most popular kind of financial tools in the Ukrainian financial market?
8. Describe the model of the financial market regulation in your country.

Practical tasks

Task 1. The state currency bonded loan is provided in the following amounts: 100 million USD per 100 000 bonds; 415 million USD per 41 500 bonds; 7 370 million USD per 73 700 bonds. Define the nominal cost of the bonds according to their value.

Methodical recommendations

The nominal cost of a bond is calculated as the ratio of the number of bonds to their total cost.

Task 2. Define the current annual income of a bond with the nominal cost of 10 000 UAH and the annual interest rate of 110 %.

Methodical recommendations

The current income is calculated using the following equation:

$$I_c = i_c \times P_n \, , \tag{7.1}$$

where I_c is the current annual income in absolute expression;

i_c is the annual interest rate (norm of profitability);

P_n is the nominal cost of a bond.

Task 3. The owner of a bond with the nominal cost of 1 000 UAH at 20 % per annum sold the paper in 146 days. Determine the coupon money which will be received by the seller.

Methodical recommendations

Coupon money can be calculated using the following equation:

$$I_{cm} = \frac{I_к \times (360 - t)}{360} \, , \tag{7.2}$$

where t is the number of days beginning from the day of selling to the current interest day (the date of payments on the coupon).

Task 4. Calculate the amount of discount and the amount paid by the Bank for bills. The Bank accounted three bills:

a) 7 200 UAH before 90 days to its maturity;

b) 5 500 UAH before 60 days to its maturity;

c) 4 500 UAH before 45 days to its maturity.

The annual interest is 10 %.

Methodical recommendations

The amount of discount (C) is calculated using the following equation:

$$C = \frac{S \times t \times d}{365 \times 100\,\%} \, , \tag{7.3}$$

where C is the amount of discount;

S is the nominal cost of a bill, UAH;

t is the period (in days) from the accounting date to the day of payment;

d is the annual interest rate.

The number of days per year is 365.

Topic 8. Finance of business entities

The aim is to form a system of theoretical knowledge as for basic categories and concepts in the field of business entities' finance, as well as practical skills in the implementation of knowledge.

The main issues

8.1. The concept and forms of business entities.

8.2. Finance of business entities in real economy.

8.3. Formation of financial institutions' resources.

8.4. Finance of nonprofit organizations.

8.5. Finance of budgetary institutions and organizations.

The competences to be formed:

knowledge:

the fundamentals of finance organization at enterprises of different forms of ownership;

the nature of financial relations of business entities;

financial features of nonprofit organizations;

skills:

to use theoretical knowledge for the organization of company financing;

to identify the ways of financial resources usage;

to determine the criteria for assessment of the financial activity performance;

communication:

the ability to analyze the main factors influencing the formation of financial resources of the entity;

the ability to find ways to improve the financial activities of economic entities;

autonomy and responsibility:

making decisions related to the financial activity of economic entities;

the ability to further deepen the knowledge of finance of business entities.

Key words: business entity, financial relations, financial resources, finance of enterprises in real economy, commercial considerations, monetary funds, financial independence, financial mechanism of an enterprise, nonprofit organization, financial institution, budget organization, cost estimation.

8.1. The concept and forms of business entities

According to part 1, Art. 55 of the Economic Code (EC) of Ukraine, *business entities* are the participants in economic relations which conduct economic activity with implementing economic competence (a set of economic rights and duties), have separate property and are responsible for their obligations within this property except cases defined by the legislation.

Business entities are the following:

economic organizations – legal entities established according to the Civil Code of Ukraine; governmental, public utilities and other enterprises established according to the Economic Code and other legal entities conducting economic activity and registered as prescribed by the law; citizens of Ukraine, foreigners and stateless persons conducting business activity and registered as entrepreneurs.

An enterprise is a business entity created for the organization of entrepreneurial activity. Its economic purpose is to ensure social needs and get profit. There are many types of enterprises (Table 8.1).

Table 8.1

Types of enterprises

Criterion	Types of enterprises
1	2
1. According to the forms of ownership	A private enterprise (company) that operates on the basis of private ownership of citizens or a legal entity; a collective enterprise which is a company operating on the basis of collective ownership; a municipal enterprise which operates on the basis of municipal property of the territorial community; a state enterprise which operates on the basis of state property
2. Depending on foreign investment in the authorized capital and its size	Enterprises with foreign investment (foreign investment must be at least 10 percent in the authorized capital of the enterprise); foreign companies (foreign investment equals 100 percent in the authorized capital)

Table 8.1 (the end)

1	2
3. Depending on the way of establishment, formation of the authorized capital and order of enterprise management	A unitary enterprise created by one founder, who provides all the necessary property, generates the authorized capital that is not divided into shares, approves the charter, shares revenues, directly or through the manager appointed by him, manages the company and forms its staff on the basis of recruitment, makes reorganization and liquidation decisions; corporate enterprises which are cooperative enterprises created in the form of economic organizations and other companies, including those based on private ownership of two or more persons
4. Depending on the number of employees and annual income	Entities of small, medium and big business

Depending on the economic sector, business entities and their business (institutional) units are divided into: public and private corporations, financial corporations, general financial administrations, nonprofit organizations serving households and households themselves.

Characteristics of business (institutional) units depending on the economic sector:

state and nonstate corporations (legal entities in the sphere of public production) – public, private, collective, leasing, joint ventures, joint stock companies, limited and additional liability companies, cooperatives and voluntary associations of businesses and professional bodies in the form of associations, consortia, corporations, concerns, tenants' organizations, etc.;

financial corporations – credit institutions, investment funds, insurance companies, nonstate pension funds, etc.;

nonprofit organizations – hospitals, schools, universities, vocational schools, creative unions, theaters, libraries, museums and others;

nonprofit organizations serving households – nongovernmental organizations (NGOs), political parties and others;

households – collecting individuals as consumers and in some cases as actors of noncorporate productive activity who receive income in order to improve their welfare.

8.2. Finance of business entities in real economy

Real economy is a set of industries which produce tangible and intangible (material and nonmaterial) goods and provide services.

The real economy covers small, medium and big enterprises of various organizational and legal forms involved in the production of material goods and their delivery to consumers. The basis of the real economy are enterprises producing industrial and agricultural products.

Finance of business entities (enterprises) is economic relations connected with formation, distribution and use of financial resources of enterprises in the process of reproduction.

Obligatory conditions for the effective functioning of enterprises' finance are the following:

variety of ownership forms;

free market pricing and competition;

availability of labour, goods, and capital markets;

legal provision of the rules of economic behavior for all entities of entrepreneurial activity;

limitation and regulation of state intervention in enterprises' activity;

freedom of entrepreneurship and independence in making managerial decisions;

interest in the results of financial and economic activity;

control over financial and economic activity of enterprises.

The basis of enterprises' finance organization is *commercial providence* (a constant comparison of costs and results of financial and economic activity that provides getting maximum profit with minimal costs). The principles of commercial providence are the following:

self-regulation which takes place when all the enterprises, except the state ones, are provided with full autonomy in decision-making and taking measures in the sphere of production, investment activity, taking into account the available financial, human and material resources;

self-repayment which means organization of financial activities in order to repay the funds invested in a company, get profit and other owned financial resources and fully implement all the obligations to suppliers of material resources, financial institutions and budget;

self-financing which means financing of not only reproduction but development for account of their own financial resources.

Finance of enterprises moves through three types of activities: operational, investment and financial.

Operational activity is a basic activity of an enterprise associated with production and sale of products (goods, works, services), which is the main purpose of the enterprise foundation and which provides the major part of its income, as well as other activities which are not covered by investment or financial activities. Operational activity is mainly aimed at the commodity market, investment and financial activities – at the financial market.

Investment activity is the purchase and realization of those noncurrent assets and financial investments that are not part of monetary equivalents. This activity is associated with the efficient investment of the outside funds. In general, investments mean all types of property and intellectual values invested in objects of entrepreneurial and other activities, resulting in profit (income).

Financial activity is an activity which leads to changes in the size and structure of company's own or borrowed capital (which is not the result of operational activity). Optimization of capital structure (optimization of funding) leads to a reduction of costs for its attraction and provides the financial basis for successful operational and investment activities.

Financial resources of an enterprise are a set of funds at the disposal of a business entity designed to perform its financial obligations and to finance actual expenses associated with economic activity. They characterize financial capacity, i.e. the enterprise's capabilities to implement costs for getting income. Financial resources of an enterprise are formed by one's own or borrowed funds.

The initial formation of financial resources occurs during the creation of business entities. For existing enterprises financial resources are formed mainly from profit (from the basic and other activities) and depreciation.

Classification of financial resources

Based on the cycle:

initial financial resources i.e. resources with which an enterprise starts its activity (authorized capital);

marginal resources obtained as a result of its activity (profit);

based on the character of use:

material financial resources invested in assets for provision of productive process (fixed capital assets);

financial resources in turnover which serve a separate productive cycle (working capital);

depending on the sources of formation:

financial resources generated at the stage of company's setting (founders' contributions to authorized capital);

financial assets created through the company' own revenues (depreciation, target revenues; gross and net income, operational income);

financial resources mobilized in the financial market (flows from shares, bonds and other securities issuance, credit investments);

financial resources received from redistribution of monetary proceeds (financial resources received from industrial bodies, associations; insurance compensation).

Financial resources can exist in the form of a fund and out of it. Monetary funds are a part of money used according to the set purpose (authorized fund, labor compensation fund, depreciation fund, saving fund, consumption fund, reserve fund, material incentive fund, social development fund). Money out of funds is used for fulfillment of financial obligations by enterprises to the budget and off-budget funds, banks, and insurance companies. Enterprises also receive grants, subsidies, sponsorship fees, bank loans in a non-fund form.

Equity is the amount of an enterprise's own money, which is the result of its activity or received from the owners or members of the enterprise in the form of contributions, purchased shares, etc. Equity capital characterizes the overall value of business entity's assets belonging to it by the right of ownership (Fig. 8.1).

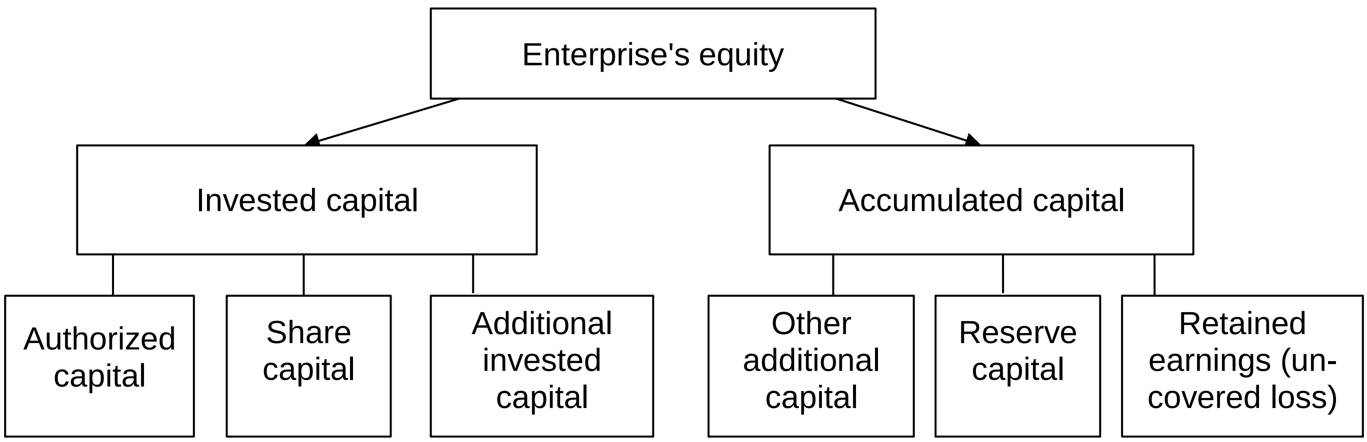

Fig. 8.1. **The components of enterprise's equity**

Invested capital is the capital formed by contributions from the enterprise owners, as well as due to the conversion of debt liabilities of the enterprise in shares. It consists of:

authorized capital (total value of assets fixed in constituent documents that is the contribution of owners (participants) to the company capital);

share capital (share contributions of the members of unions and other companies, if it is provided by constituent documents);

additional invested capital (the amount by which the selling price of the shares issued exceeds their nominal value (for joint stock companies); the amount of capital contributed by the founders over the authorized capital (for other companies)).

Accumulated capital is capital gained in the process of economic and financial activities of a business entity. The following types of accumulated capital are distinguished:

other additional capital (the cost of free fixed-capital assets received from other legal entities and individuals, etc.);

reserve capital (the volume of reserves established in accordance with the laws or the constituent documents from retained earnings of the company);

retained earnings (uncovered losses) that is net profit for the period which is the subject for distribution.

Enterprise income (revenues) is an increase in economic benefits in the form of reduction of additional assets or liabilities which leads to an increase of equity (excluding equity growth at the expense of owners). It includes:

operating income (income from sales and other operating income);

financial income (including income from investment in equity, other financial income: receivable dividends and interests, other income from financial transactions);

other income from operating activity (including proceeds from sale of foreign currency, revenue from sale of current assets (excluding financial investments), income from operating leasing of assets, income from exchange rate difference on transactions in foreign currency, received fines, penalties and other sanctions for violations of economic agreements, income from the write-off of accounts payable, received grants and subsidies, and other revenues);

extraordinary income (including insurance reimbursement, money transferred for an enterprise to finance losses from other sources (public authorities, businesses and individuals, finance of foreign business, etc.).

Enterprise expenses (costs, losses) are a reduction in economic benefits in the form of an flow-out of assets or liabilities increase that result in the decrease of equity (excluding equity reduction due to its withdrawal or distribution by owners).

Operating expenses cover costs and expenses associated with production and sale of goods (basic activity) and also conducting operations for their provision (other activities). These are: costs of production, selling, administrative and other operating expenses.

Financial expenses are expenses which appear as a result of interest payment related to the involvement of creditors' equity. They cover interest on credits and other financial expenses.

Losses on investments accounted for using the equity method reflect losses of an enterprise from investment in subsidiary companies or joint ventures.

Profit is a form of financial resources, gained by an enterprise as a result of its economic activity.

The principles of profit distribution are:

provision of primary obligations to the state;

stimulation of interest in better economic results;

creating favorable conditions for business entities whose activities have purely economic and social value for investors.

Distribution of business entity's profit is implemented in two steps.

Firstly, total income is distributed. At this stage, participants are the state and the enterprise. The proportions of profit distribution between the state (budget) and the enterprise are formed by such factors as definition of tax bases, tax rates, tax incentives.

Secondly, profit after taxation is distributed and used.

8.3. Formation of financial institutions' resources

Typical services of financial institutions are: taking deposits from public and other funds to be returned; provision of loans; providing financial leasing; money transfer; consumer credit, mortgage credit, factoring with or without regress; financial guarantees or obligations; trade transactions with money market tools (checks, bills, certificates of deposit, derivatives etc.); foreign currency; exchange instruments, securities and bank interests; trade in futures goods; participation in securities issuance; individual and collective securities portfolio management; storage and administration of cash or liquid securities on behalf of others; organization of life insurance and other insurance-related investment.

The types of financial institutions are given in Fig. 8.2.

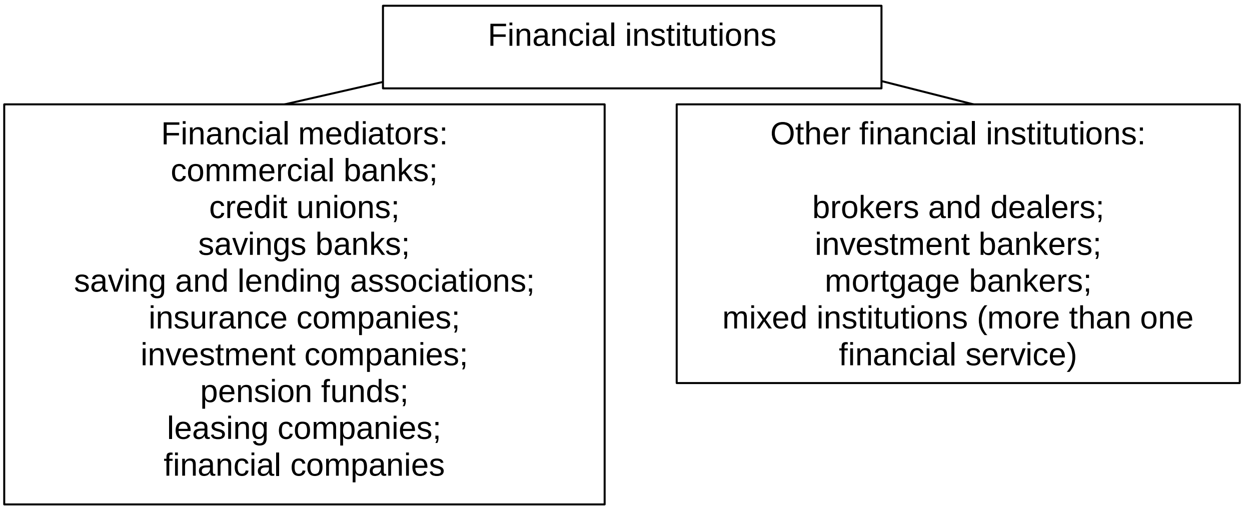

Fig. 8.2. **The types of financial institutions**

Bank finance is a set of financial relations of a bank arising in the process of equity formation, accumulation of separate funds which are placed on accounts of business entities and individuals, budget and target funds, their transformation and use by ensuring the movement of financial flows in order to achieve the required level of profitability and liquidity.

The types of bank financial relations are:

between the founders at the time of bank establishment – financial relations arising during the authorized (share) capital formation;

between the bank and its customers – financial relations arising during provision of banking services and products, the acquisition of IT software, fixed-capital assets, distribution and redistribution of income;

between the bank and its units (branches, departments) – financial relations as for the formation and allocation of financial resources, financing expenses;

between the bank and its employees;

between banking institutions and the National Bank of Ukraine – financial relations arising during the formation, distribution and use of centralized target funds and reserves, financing target programs, conducting market and scientific research;

between the bank and the state financial system – payment of taxes to the budget, formation of extra-budgetary funds, provision of tax incentives;

between the bank and other financial mediators.

In terms of financial flows, *bank financial activity* should be divided into two parts: passive and active operations. Passive operations are operations that attract funds by receiving deposits, issuance of its own securities, borrowing from other banks. This leads to the appearance of bank liabilities to the owners of resources. Formation of their own funds at the expense of increasing authorized capital, replenishment of reserve and special funds are also passive operations. Active operations are operations on the placement of funds by granting loans (credits), securities, currencies, purchase of precious metals, etc.

8.4. Finance of nonprofit organizations

A nonprofit organization is a separate autonomous business entity with a legal person whose main objective is not to make a profit for its further distribution between participants of this organization.

The following entities belong to nonprofit organizations:

budget institutions and organizations, i.e. those which are kept at the expense of the budgets;

public associations (unions, political parties, credit unions, religious organizations), pension funds, business associations, creative unions, etc.;

charities, cultural and other target public funds.

The main activity of nonprofit organizations is provision of charitable assistance, educational, cultural, scientific and other services for public consumption, establishment of a social provision system for citizens, and other purposes divided by statutory documents.

Finance of nonprofit organizations is socioeconomic relations which have monetary nature and appear in the process of formation, distribution and use of funds related to the implementation of their public activity.

The types of nonprofit organizations' financial relations are:

with local governments and public authorities – concerning the receipt and use of budgetary funds, taxes, fees for obligatory pension and social insurance;

with individuals and organizations – for formation of extra-budgetary revenue (membership and equity contributions, contributions of the founders, target receipts, including donations, grants, and income from entrepreneurial activities) and their further use;

with employees – concerning the formation and use of labour compensation and social development funds.

8.5. Finance of budgetary institutions and organizations

According to the Budget Code of Ukraine *a budget institution* is a body, institution or organization defined by the Constitution of Ukraine, as well as an institution or organization created in accordance with the established procedure by state authorities or local governments, which is fully kept at the expense of the state or local budgets.

The purpose of establishing and the main activity of budget institutions do not provide getting profit.

Regulation of financial relations of economic entities in the budgetary sphere is carried out by the following legislative acts: the Constitution of Ukraine, the Budget Code of Ukraine, the law of Ukraine "On the State Budget for the Current Year", other legal acts.

Financial resources of a budget institution are monetary funds of the designed purpose which exist in the form of savings and income and are formed in the process of distribution and redistribution of national wealth, gross domestic product and national income, concentrated in budget institutions and used according to the main directions of such organizations' activities.

Budgetary institutions have practically no their own revenues and operate at the expense of budgets. *The list of paid services that may be provided by a budget institution, is established by the Cabinet of Ministers of Ukraine.*

The main sources of budget organizations' financial resources are: funds of budgets of different levels; funds of state extra-budget funds; income from entrepreneurial activity.

Depending on the nature of financial activities, budgetary institutions can be divided into four groups:

institutions of budget financing (services are free);

divisions of budget institutions on cost accounting which are not separate legal entities (payment for services is provided on a contractual basis and in the form of tariffs);

institutions working on cost accounting with a low level of profitability (payment for services covers costs, salary of staff, etc.);

institutions working on cost accounting with a high level of profitability (payment services allow them to develop).

In practice only two methods of budgetary financing are used:

1) financing by the "net budget" system, in which budget funds are allocated on a fairly limited range of costs listed in the budget institution;

2) financing by the "gross budget" system, in which budget funds are available for all types of expenditures in both current and general form.

Budgetary institutions are financed in the following forms:

budget investments which can take the form of capital investment, project financing of a particular investment project and purchase of shares or rights of participation in the enterprise management;

budget credits is provision of funds from the budget to business entities on a returnable and paid basis; they differ from bank loans by slightly low level of interest rates and more favourable conditions;

estimated financing which refers to the budgetary allocation on the basis of a special planning and financial document – the budget (estimate);

government transfers i.e. non-repayable and irreversible payments from the budget to legal entities that are not intended for the purchase of goods or services, provision of credit or payment of an outstanding debt.

Questions for self-assessment

1. Give a definition of a business entity.
2. What is an enterprise and what types of enterprises exist?
3. What is financial resources of a business entity?
4. What monetary funds can any enterprise have?
5. What structure does an enterprise's equity have?
6. Explain the essence of commercial providence.
7. What types of activity can be conducted by enterprises?
8. Name the principles of profit distribution for a company.
9. Describe the features of budget institutions' financing.
10. What kind of financial institutions are popular in your country?

Practical tasks

Task 1. Determine the net revenue from sales, financial results before taxation (pretax accounting income), net profit and distribute it, return on sales using the following data: revenue from sales (including VAT) is 1860 thousand UAH; cost of sold products is 1100 thousand UAH; non-operating income is 85 thousand UAH; income from financial and investment operations is 54 thousand UAH; losses from emergencies are 18 thousand UAH; cost of sales is 16 thousand UAH; profit taxes are 200 thousand UAH. Deductions from net profit make: 25 % payment to the founders; 15 % to the reserve fund; 60 % – other payments.

Task 2. Calculate revenue from sales (including VAT) using the following data (Table 8.2).

Table 8.2

The production and selling data

Product name	Residuals at the beginning of the year, items	Produced products, items	Residuals at the end of the year, items	Cost per item, UAH	Return on sales, %
A	120	1700	100	250	10
B	170	2000	80	290	17
C	250	3000	190	350	15

Task 3. Calculate the gross income based on the cost of production per 1 UAH using the following data: revenues from sales in wholesale prices in the basis period are 320 thousand UAH; the full costs of production are 260 thousand UAH. It is planned to reduce the cost per 1 UAH of products by 0.04 UAH. The planned revenues from sales in wholesale prices are 365 thousand UAH.

Task 4. Last year Iceberg Ltd produced 6 000 units of products. Price per unit of the product was 122.5 UAH, its total costs of production and sale are 104.36 UAH. The ratio of direct and fixed costs for this type of product is 55 % and 45 % respectively. Calculate the break-even point for this production in volume and value terms. Define profit and return on sales. Assess the reserve of financial strength for the company.

Task 5. Determine the level of debt security (DS) if, according to the balance sheet on 1 January of the current year, the sum of equity is 540 thousand UAH, long-term liabilities amount to 340 thousand UAH, and current liabilities make 260 thousand UAH.

Topic 9. International finance

The aim is to create a comprehensive understanding of a set of relations on funds, capital creation and use necessary for the functioning of global financial markets.

The main issues

9.1. The concept, purpose and functions of international finance.

9.2. The general characteristics of the global financial market and its structure.

9.3. International corporations and international financial institutions.

The competences to be formed:

knowledge:

the fundamentals of organization and functioning of the global financial system; the essential characteristics of the global financial market and its structure; organization of international financial institutions' activities, their relations and information support;

skills:

analysis of the sources of international corporations' finances;

arranging/effecting international settlements;

communication:

the ability to define the essence of international finance and basics of organization;

the ability to analyze the main factors that affect the functioning of the structural elements of the global financial market;

the ability to justify peculiarities of functioning and development of the international financial institutions;

autonomy and responsibility:

making decisions on identifying priority directions of international finance development;

implementation of advanced international experience of the practice of financial relations in Ukraine.

Key words: globalization of the financial market, the global financial market, global financial environment, international finance, the subjects of international finance, the international financial corporation, the international financial center, international financial institutions.

9.1. The concept, purpose and functions of international finance

International finance is a system of complicated relations on the creation and use of funds necessary for the implementation of foreign economic activity of states, firms, others legal entities and individuals.

The factors of international finance development are the following:

appearance of global markets;

deepening of the international labour division, migration of the labour force;

internationalization and globalization of economic relations;

development of international trade of goods and services;

development of currency systems and strengthening of mutual influence of currency on their costs;

increase of capital movement from one country to another;

establishment of international financial corporations;

development of the international financial market;

development of international programs of various types and necessity of their functioning: humanitarian, cultural, political.

The elements of international finance are:

international settlements – monetary settlements between the subjects of international activities that are associated with the movement of inventory and services in international circulation;

international financial markets and mechanisms for trading in specific financial instruments – currency, loans, securities;

international taxation as a method of mobilization of funds;

international financial management as a system of economic decisions on the definition of sources and direction of financing in transnational corporations, decrease of financial risks under the conditions of internationalization of economic life. The main place in international financial management is given to the transnational financing, international investment, risk management.

The purpose of international finance is to serve effectively the inter-state movement of goods and services and redistribution of money and capital between competing agents of the world market, as well as to signalize about the status of the global financial conditions in time.

The object of international finance is the cost of: funds of international institutional organizations; the international loan fund; international investments; monetary instruments involved in international relations (national currencies, securities of states, multinational and national corporations, etc.); international trade and services.

The subjects of international interaction are given in Fig. 9.1.

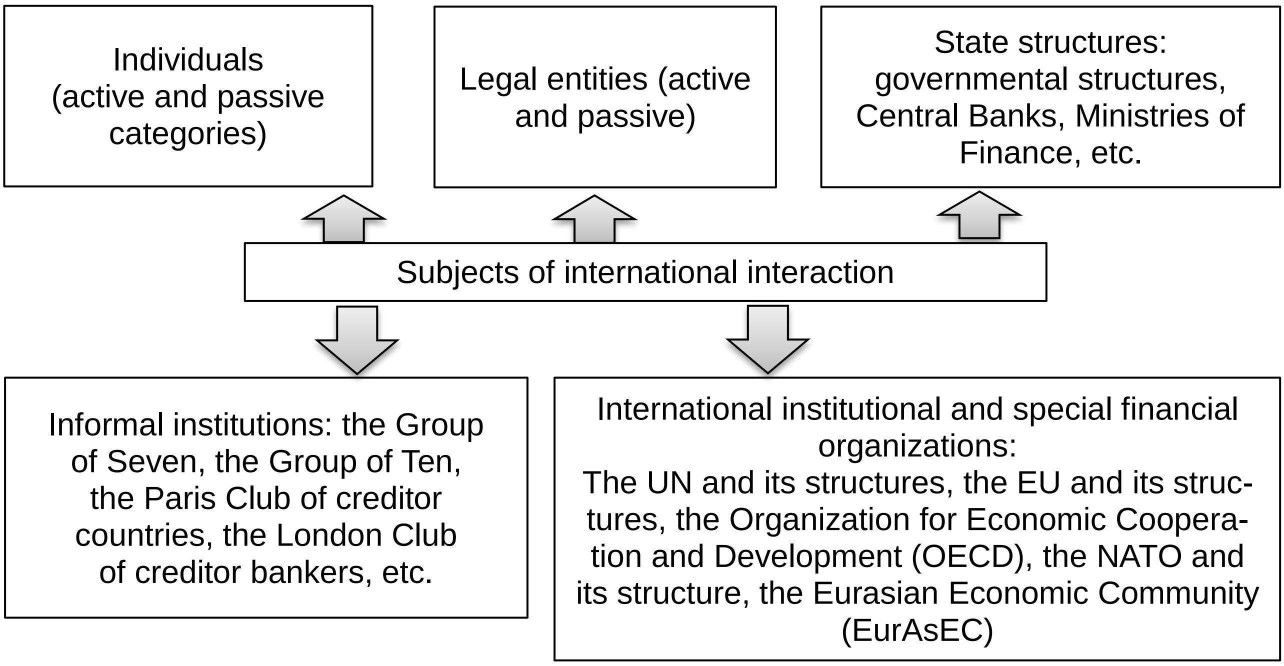

Fig. 9.1. **The subjects of international interaction**

International monetary and financial flows are the flows of foreign currencies or any other financial assets due to economic activities of subjects of the world economy.

They are formed between different countries in the form of:

a) cash flows – currency revenues from exports of goods and services and payment for imported goods and services. These flows can reflect the finances of business entities. Cash flows of legal entities belonging to different countries reflect the movement of money between countries;

b) flows of credit funds, which are also two-way: on the one hand, providing with a loan, on the other hand – its repayment and payment of interest. Thus, on the basis of these flows the movement of financial resources between countries takes place. Their distribution is regulated, firstly, by the exchange rate and, secondly, by customs tariffs and regulations.

The main directions of international financial transactions are:

foreign exchange operations;

attraction of foreign investments;

mobilization of foreign loans;

carrying out insurance with foreign insurance companies;

provision of financial assistance.

International payments are the system of implementation of monetary claims and liabilities appearing between the subjects of foreign economic activity based on the exchange of relevant objects. Forms of international payments are: cash and non-cash (incashment, letters of credit, bank transfer, bills, bank guarantee, barter, etc.).

9.2. The general characteristics of the global financial market and its structure

The global financial market is a set of continuous operations on purchase and sale of financial instruments (currencies, international securities, credit and insurance products) in the global world economic space.

The main purpose of the global financial market is to ensure the redistribution of saved free financial resources between countries in the national markets for sustainable economic development of the world economy and receiving a certain income from these operations.

The biggest differences between global and national financial markets are:

a huge scale (daily transactions in global financial markets exceed the transactions of world merchandise trade more than 50 times);

lack of geographical boundaries;

round-the-clock operations;

use of the currencies of leading countries;

participants in the global financial markets are mostly first-class banks, corporations, financial and credit institutions with high ratings;

access to these markets is open primarily for the first-class borrowers or under sustainable guarantees;

specific international interest rates;

standardization and a high degree of informational technologies of paperless transactions based on computer usage.

Factors affecting the formation of the global financial market are:

a) the increase of external operations at the national and regional financial markets;

b) appearance of new ways of mobilization of capitals;

c) universalization and diversification of the activities of transnational banks and corporations.

An international financial center is a place of concentration of banks, specialized credit and financial institutions engaged in international currency, credit, financial transactions, transactions with securities and gold.

London is the leading center of the Euro currency, *Tokyo* is the market of bonds (due to large amounts of savings and surplus of capital in Japan), *Zurich* is the leading market of foreign bonds (due to the anonymity of foreign deposits).

Other international financial *centers* are: Frankfurt, Amsterdam, Paris, Hong Kong, the Bahamas, the Cayman Islands; they perform various functions associated with global capital flows.

The functions of the global financial market are:

1. The accumulation of cash flows in the form of savings and investments.
2. Formation of prices of financial instruments.
3. Regulation of international financial flows.

Table 9.1 describes the possible participants in the global financial market.

Table 9.1

The participants in the global financial market

Feature	Types of participants
1	2
1. The character of action in operations	Direct participants are stock exchange members of related derivatives markets who enter agreements at their own expense and/or at the expense and on behalf of the clients who are not members of the exchange; indirect participants are participants who are not members and therefore have to seek the services of direct market participants
2. The aims and motives of action	Hedgers are participants of the world financial market who use the derivatives market to cover the exchange rate (price) risk, risk transfer. Speculators enter into an agreement for the purpose of benefit from the favorable dynamic of rates

Table 9.1 (the end)

1	2
3. The types of issuers and their characteristics	International agencies (the World Bank, the International Bank for Reconstruction and Development); national governments and sovereign borrowers; provincial and regional authorities (state administrations); municipal authorities; quasi-public issuers; corporations, banks and other organizations
5. The type of investors	Private; institutional

The offshore market ("offshore" means "beyond the coast") is the market of offshore zones and territories. Offshore zones are countries (or part of their territory), within which a special regime of activity, registration and taxation is established for the residents of this country:

almost full exemption from state control over a company, complete privacy is guaranteed;

accelerated and simplified procedure for registration of non-resident (for this country) companies;

taxes on profits of non-resident companies are paid at cut rates.

Offshore centers have the following special features:

internal political stability to ensure continuity of operations;

minimal governmental regulation and incentives for nonresidents wishing to work in the market;

a functional banking system, implementing international agreements;

lack of international regulation;

availability of qualified staff and communications for effective interaction with the international banking community.

Five major sectors of the international financial sector are: currency, credit, stock, investment, insurance. Their boundaries are quite mobile, so a lot of tools of modern international financial market combine the elements of several market sectors.

9.3. International corporations and international financial institutions

Transnational corporations (TNCs) are the national monopolies with foreign assets, production and trade marketing whose activity goes beyond one state.

Financial flows of transnational corporations are the circulation of financial assets and liabilities which have cross-border nature, are multicurrency, multilevel (combination of money of foreign branches and resources of TNCs as a whole), integrate (presence of rigid linkages of financial flows).

Internal financial resources of TNCs provide opportunities for the financing of specific projects, the development of the whole corporate structure and its components (Fig. 9.2). They are quite easy to operate at the level of corporate management, relatively easy and quickly activated, which provides their significant ratio in the assets of many foreign TNCs.

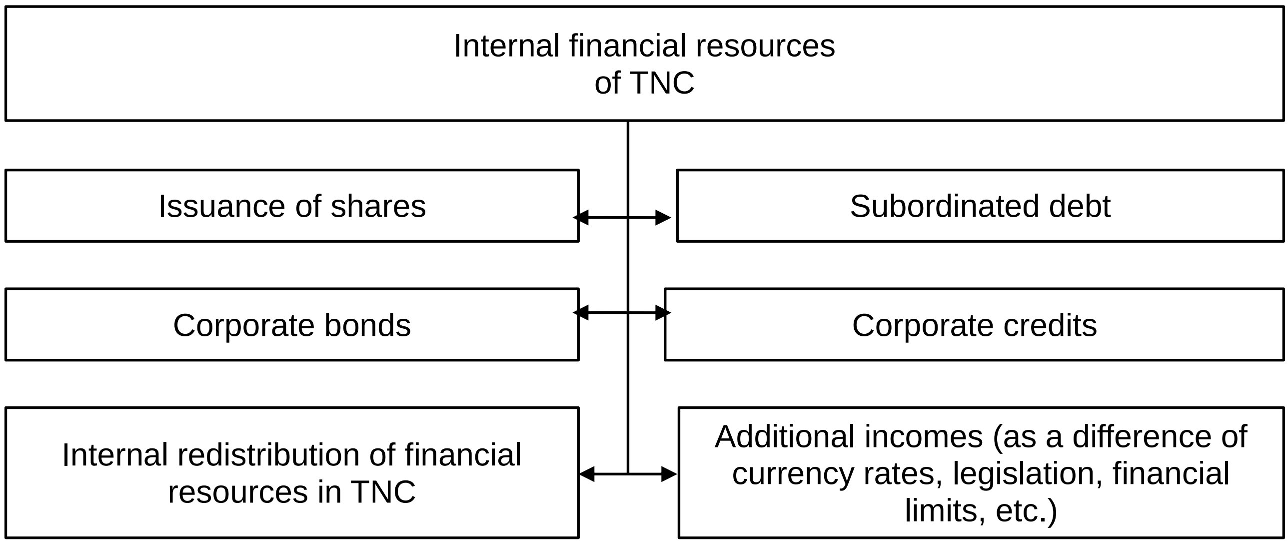

Fig. 9.2. **Ways to attract TNC financial resources**

An *international financial institution (IFI) is* a financial institution that has been established (or chartered) by more than one country, and hence is a subject of international law. Its owners or shareholders are generally national governments, although other international institutions and other organizations occasionally figure as shareholders. The most prominent IFIs are creations of multiple nations, although some bilateral financial institutions (created by two countries) exist and are technically IFIs. The best known IFIs were established after World War II to assist in the reconstruction of Europe and provide mechanisms for international cooperation in managing the global financial system.

Today, the world's largest IFI is the European Investment Bank, with a balance sheet size of €512 billion in 2013. This compares to the two components of the World Bank, the IBRD (with assets of $358 billion in 2014) and the IDA (with assets of $183 billion in 2014). For comparison, the largest commercial banks have assets of $2,000 – 3,000 billion each.

Other international financial institutions are:

the Bretton Woods Institutions (the International Monetary Fund and the World Bank);

the Bank for International Settlements (BIS);

Banks of Regional Specialization (the African Bank of Development, the Asian Bank of Development, the European Bank for Reconstruction and Development, London and Paris Clubs of Creditors, etc.).

Leading international organizations are: the United Nations, the European Union.

Questions for self-assessment

1. Give a definition of international finance.
2. What operations with money belong to the international finance?
3. Name the subjects of international interaction.
4. Name the biggest international financial centers.
5. Name the participants in the international financial market.
6. Explain the status of the offshore zones and centers.
7. Define the main directions of conducting international financial transactions.
8. What are the peculiarities of financial flows of transnational corporations?
9. What for are international financial institutions established? What is their purpose?
10. What international financial institutions do you know?

Practical tasks

Task 1. The Bank has established the following quotation of rates for USD/UAH: buying – 11.45; selling – 11.95. Determine how much money in UAH will be received in exchange for 15 000 dollars and how many dollars will be received in exchange for 1 million hryvnias.

Task 2. In the London Bank the rate of the US dollar to Euro is the following: buying – 1.559; selling – 1.5936. Determine how many euros you can get in exchange for $10 000 and how many dollars you can get in exchange for 10 000 euros.

Task 3. A bank located in the United States has established the following currency rates: US dollar/Euro: 5.42/5.51 and the Japanese yen/Euro: 3.62/3.67. Determine the cross-rate of purchase and sale of dollar to yen.

Methodical recommendations

The cross-rate is the ratio between two currencies (neither of which is the USA dollar) that is determined on the basis of rates for these currencies relative to the third, usually the USA dollar.

In direct quotation it is the exchange rates of *A* and *B* related to the currency *C*.

	Buying	Selling
A/B	R_{AB1}	R_{AB2}
C/B	R_{CB1}	R_{CB2}

In this case *A* is dollar, *B* is euro, *C* is yen. Then the cross-rate of currency *A* to currency *C* will be established according to the following equation:

$$\text{buying} = \frac{R_{AB1}}{R_{CB1}}, \tag{9.1}$$

$$\text{selling} = \frac{R_{AB2}}{R_{CB1}}. \tag{9.2}$$

Task 4. The Bank has set the following currency rates: the USA dollar/hryvna rate is 11.45/11.95 and the USA dollar/rouble rate is 34.5/32. Determine the cross-rate of purchase and sale of the Ukrainian hryvnia to the Russian rouble.

Methodical recommendations

In this case currency *A* is dollar, *B* is hryvnia, *C* is rouble. There are the following rates according to the direct quotation:

	Buying	Selling
A/B	R_{AB1}	R_{AB2}
A/C	R_{AC1}	R_{AC2}

The cross-rate will be defined using the following equation:

$$\text{buying } \frac{B}{C} = \frac{R_{AC1}}{R_{AB2}}, \tag{9.3}$$

$$\text{selling } \frac{B}{C} = \frac{R_{AC2}}{R_{AB1}}. \tag{9.4}$$

Task 5. The following exchange rates are known: Japanese yen/US dollar 1.651/1.648 and US dollar/hryvnia 11.45/11.87. Determine the cross-rate of buying and selling of yen to hryvnia.

Methodical recommendations

	Buying	Selling
A/B	R_{AB1}	R_{AB2}
B/C	R_{BC1}	R_{BC2}

Then the cross-rate of *A* to *C* will be defined as:

$$\text{Buying} = R_{AB1} \times R_{BC1}, \tag{9.5}$$

$$\text{Selling} = R_{AB2} \times R_{BC2}. \tag{9.6}$$

Task 6. The volume of domestic exports is \$62 billion, import is \$65 billion. The volume of exports of all foreign countries is \$6 750 billion, import is \$6 550 billion. Calculate the world trade turnover, the domestic turnover, its share in the world trade, the trade balance.

Methodical recommendations

To calculate the trade turnover use the following equation:

$$TO = E + I, \tag{9.7}$$

where *TO* is the trade turnover;

E is export for a certain period of time (mostly a year);

I is import for this period of time (a year).

The trade balance is the difference between the export and import of a certain country:

$$TB = E - I, \tag{9.8}$$

where *TB* is the trade balance.

Trade balance can be passive if $I > E$ and $TB < 0$, and active if $I < E$, and $TB > 0$. It is important for any country to get an active trade balance.

Topic 10. Financial management

The aim is to create a comprehensive understanding of financial management in the enterprise management system; to obtain theoretical knowledge of the basic principles of formation, distribution and use of financial resources at an enterprise, the system of financial management objectives, formation of strategy and tactics of financial management; to identify the components of the financial management mechanism.

The main issues

28.1. The essence and functions of financial management in the business management system.

28.2. The goal and objectives of financial management.

28.3. Strategy and tactics of financial management.

28.4. The financial management mechanism and its components.

The competences to be formed:

knowledge:

the place and role of financial management in the enterprise economic activity management;

the components of the financial management mechanism;

skills:

to form the main goals and objectives of financial management at an enterprise;

to make strategy and tactics of financial management at an enterprise;

to select and apply financial methods;

to collect economic and financial information from internal and external sources;

communication:

the ability to define the essence of financial management;

the ability to analyze the main factors affecting the financial activities of an enterprise;

autonomy and responsibility:

definition of the features and priority directions of the enterprise financial activity development;

identification of negative factors influencing the enterprise financial activity.

Key words: financial management, financial resources, financial strategy, financial tactics, financial policy, financial tools.

10.1. The essence and functions of financial management in the business management system

Businesses need finance to meet their requirements in economic world. Any kind of business activity depends on the finance. Hence, it is called life-blood of a business organization. Whether the business is big or small, it needs finance to fulfill its business activities.

What is business finance? According to [39; 47], it is the following:

business finance is a business activity which concerns the acquisition and convertion of capital funds to meet financial needs and gain overall objectives of a business enterprise.

Business finance can broadly be defined as an activity concerned with planning, raising, controlling, administering of funds used in business.

Business finance deals primarily with raising, administering and disbursing funds by privately owned business units operating in nonfinancial fields of economy.

What is corporate finance? In [39] it is defined as follows:

corporate finance is concerned with budgeting, financial forecasting, cash management, credit administration, investment analysis and fund procurement of business and business needs to adopt modern technology and application suitable to the global environment.

Corporation finance deals with the financial problems of corporate enterprises. These problems include the financial aspects of the promotion of new enterprises and their administration during early development, the accounting problems connected with the distinction between capital and income, the administrative questions created by growth and expansion, and finally, the financial adjustments required for the bolstering up or rehabilitation of a corporation which has come into financial difficulties.

Financial management is an integral part of overall management. It is concerned with the duties of financial managers in business firms. There are plenty definitions of the concept "financial management", the most popular ones are given in Table 10.1.

Table 10.1

Definition of the concept "financial management"

Author	Definition
E. Solomon	Financial management is concerned with the efficient use of an important economic resource namely, capital funds
S. C. Kuchal	Financial management deals with procurement of funds and their effective utilization in business
B. Howard and M. Upton	Financial management is an application of general managerial principles to the area of financial decision-making
J. Weston and E. Brigham	Financial management is an area of financial decision-making, harmonizing individual motives and enterprise goals
J. Massie	Financial management is the operational activity of a business that is responsible for obtaining and effective utilization of the funds necessary for efficient operations

Financial management is the process of managing the formation, distribution and use of financial resources of an enterprise and optimization of its cash turnover.

Financial management can be classified according to various criteria:

a) the level:

financial management at the microlevel (financial management of households, businesses, banking institutions, insurance companies and others);

financial management at the macrolevel (budget management, fiscal management, monetary management, etc.).

b) based on the object of management, financial management can be classified according to various schemes, in particular:

current and noncurrent assets financial management;

the owned and borrowed capital financial management;

cash and financial flows management;

anticrisis financial management;

management of various types of financial risks, particularly currency risk, risk of late payment, risk of declining asset values, etc.

The scope of financial management

1. Financial management and economics. Economic concepts like micro- and macroeconomics are directly applied with the financial management approaches. Investment decisions, micro- and macroenvironmental factors are closely associated with the functions of financial managers. Financial management also uses the economic equations like the money value discount factor, economic order quantity, etc.

2. Financial management and accounting. Accounting records include financial information of a business. Hence, we can easily understand the relationship between financial management and accounting. In early periods, both financial management and accounting were treated as the same discipline and then have been merged as management accounting because this part is very much helpful to finance managers in taking decisions. But nowadays financial management and accounting are separate and interrelated disciplines.

3. Financial and production management. Production management is the operational part of a business, which helps to multiple the money into profit. Profit of the firm depends upon the production performance. Production

performance needs finance, because the production department requires raw materials, machinery, wages, operating expenses, etc. These expenditures are decided upon and estimated by the financial department and the finance manager allocates the appropriate finance to the production department. The financial manager must be aware of the operational process and finance required for each process of production activities.

4. Financial management and marketing. Produced goods are sold in the market with the use of innovative and modern approaches. For this, the marketing department needs finance to meet their requirements. The financial manager or the finance department is responsible for allocation of the adequate finance to the marketing department. Hence, marketing and financial management are interrelated and depend on each other.

5. Financial management and human resources. Financial management is also related with the human resources department, which provides manpower to all the functional areas of management. The financial manager should carefully evaluate the manpower requirements of each department and allocate finance to the human resource department for wages, salary, remuneration, commission, bonuses, pensions and other monetary benefits. Hence, financial management is directly related with human resource management.

The purpose of financial management covers the following things:

1) financial planning (financial management helps to determine the financial requirements of a business and leads to financial planning of the firm; financial planning is an important part of business which helps to promote an enterprise);

2) acquisition of funds (financial management involves the acquisition of the required finance to a business; acquiring the needed funds plays a major role in financial management which involves all possible sources of finance at a minimum cost);

3) proper use of funds (proper use and allocation of funds leads to the improvement of the operational efficiency of a business; when the finance manager uses the funds properly, they can reduce the cost of capital and increase the value of the firm);

4) making financial decisions (financial management helps to take sound financial decisions in business; the financial decisions will affect the

entire business operation, because there is a direct relationship with various department functions such as marketing, production, personnel, etc.);

5) improvement of profitability (profitability of an enterprise purely depends on the effectiveness and proper utilization of funds by a business; financial management helps to improve the profitability position of a business with the help of strong financial control tools such as budgetary control, ratio analysis, cost and profit analysis);

6) promoting savings (savings are possible only when the business earns higher profits and maximizes wealth; effective financial management helps to promote and mobilize individual and corporate savings).

The finance manager performs the following major functions (Fig. 10.1):

1. Forecasting financial requirements. It is the primary function of a finance manager. He is responsible for estimation of the financial requirement of a business. He should estimate, how much finances are required to acquire fixed assets and forecast the amount needed to meet the working capital requirements in future.

2. Acquiring necessary capital. Having defined the financial requirements, the finance manager should concentrate on how the finance is mobilized and where it is available. It is also highly critical in nature.

3. Investment decision. The finance manager must carefully select the best investment alternatives and consider the reasonable and stable return on the investment. He must be well-versed in the field of capital budgeting techniques to determine the effective utilization of investment. The finance manager must concentrate on the principles of safety, liquidity and profitability while investing capital.

4. Cash management. Present days' cash management plays a major role in the area of finance because proper cash management is not only essential for effective utilization of cash but it also helps to meet the short-term liquidity position of a firm.

5. Interrelation with other departments. Finance manager deals with various functional departments such as marketing, production, personnel, research and development, etc. Finance manage should have sound knowledge of not only finance but be also well-versed in other areas. He must maintain a good relationship with all the functional departments of a business organization.

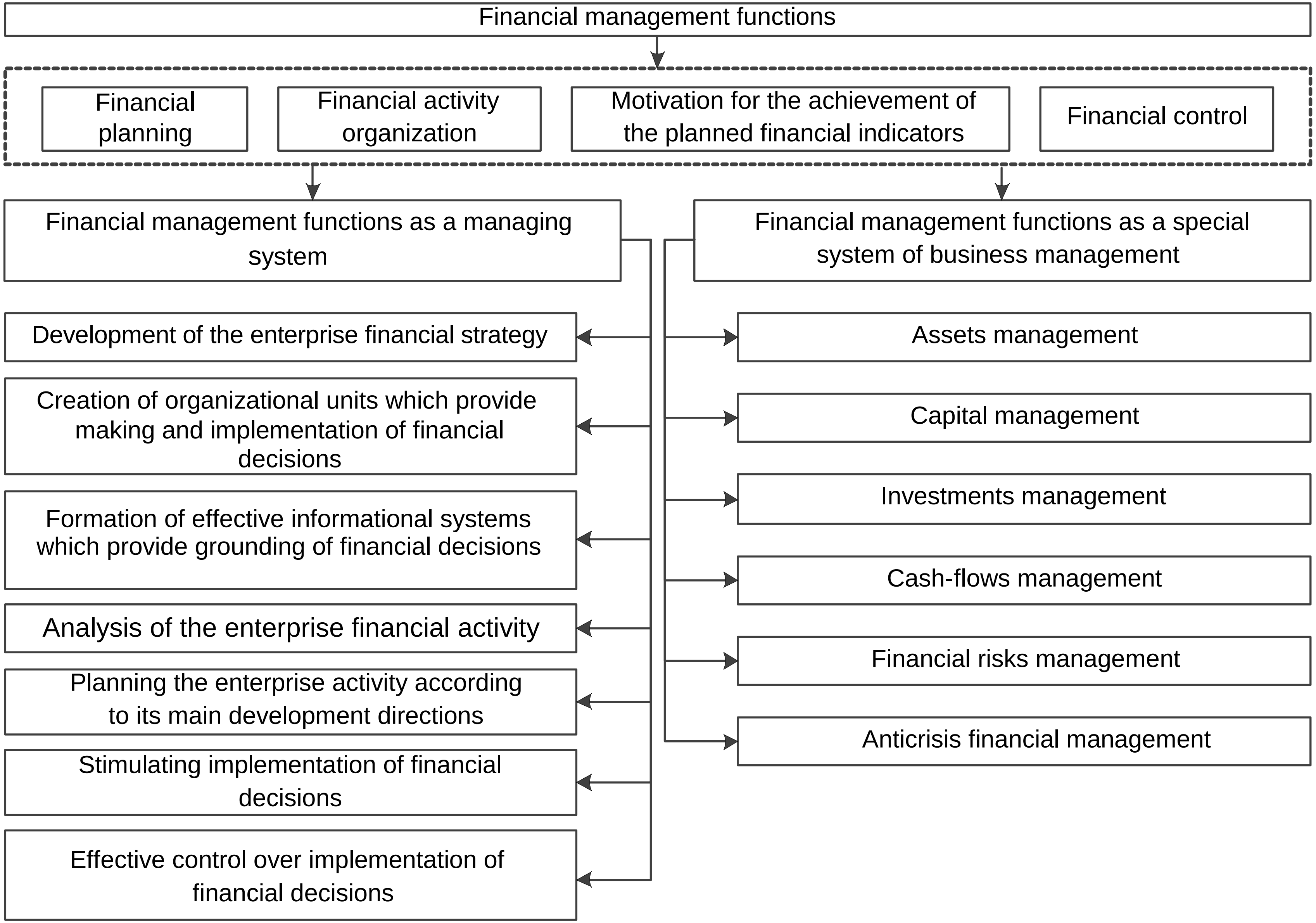

Fig. 10.1. **The financial management functions**

10.2. The goal and objectives of financial management

The objectives of financial management may be broadly divided into two parts such as: profit maximization and wealth maximization.

The main goal of any kind of economic activity is to earn profit. A business also functions mainly for the purpose of earning profit. Profit is the measuring technique used to assess the business efficiency. Profit maximization is characterized by the following important features.

1. Profit maximization is also called cashing per share maximization. It aims to maximize the business operation for profit maximization.

2. The ultimate goal of a company is to earn profit, hence, it considers all the possible ways to increase the profitability.

3. Profit is a parameter of measuring the efficiency of a business. So it shows the entire position of a company.

4. Profit maximization objectives help to reduce the risk of a business.

The following important points are in support of the profit maximization objectives of a business:

the main goal is to earn profit;

profit is a parameter of business operation;

profit reduces risk of a business;

profit is the main source of finance;

profitability also meets social needs.

The following important points are against the objectives of profit maximization:

profit maximization leads to exploiting employees and consumers;

profit maximization creates immoral practices such as corruption, unfair trade practice, etc.

profit maximization objectives lead to inequalities among the stakeholders such as customers, suppliers, public shareholders, etc.

The profit maximization objective has certain drawbacks:

It is vague: in this objective, profit is not defined precisely or correctly. It creates some unnecessary opinion regarding earning rules of a business.

It ignores the time value of money: profit maximization does not consider the time by value of money or the net present value of the cash flow. It leads to certain differences between the actual cash flow and the net present cash flow during a particular period.

It ignores risk: profit maximization does not consider any risk of a business. Risks may be internal or external which will affect the overall operation of a company.

Wealth maximization is one of the modern approaches. The term "wealth" means shareholders' wealth or wealth of the persons who are involved in business.

Favourable arguments for wealth maximization are:

wealth maximization is superior to the profit maximization because the main goal of business under this concept is to improve the value or wealth of its shareholders;

wealth maximization considers the comparison of the value to cost associated with the business. Total value is determined based on the total cost incurred for business operation. It provides extract value of a business;

wealth maximization considers both time and risk of a business;

wealth maximization provides efficient allocation of resources;

it ensures the economic interest of the society.

Unfavourable arguments for wealth maximization are:

wealth maximization leads to a prescriptive idea of a business but it may not be suitable to present-day business activities;

wealth maximization is nothing. It is also profit maximization. It is an indirect name of profit maximization;

management alone has certain benefits;

the ultimate aim of the wealth maximization objectives is to maximize profit;

wealth maximization can be activated only with the help of the profitable position of a business.

The general goals of financial management are given in Fig. 10.2.

Fig. 10.2. **Financial management objectives**

To achieve these goals financial management should carry out the following tasks:

ensuring the formation of sufficient financial resources in accordance with the objectives of the enterprise development in the future;

the most efficient use of financial resources;

cash flow optimization;

optimization of expenses;

ensuring maximization of the enterprise's profits with an acceptable level of financial risk and ensuring minimization of the financial risk level with the predicted level of profits;

constant financial balance of the enterprise;

ensuring target profitability and sustainable growth of economic potential;

avoiding bankruptcy (anticrisis management).

10.3. Strategy and tactics of financial management

There are many different ways of understanding what sustainability means in the development context. Benefit sustainability means that the benefits of development work continue to be felt by communities and individuals, whether or not the project or program continues. Organizational sustainability means that the organization is able to continue to perform its work. It has a vision and financial and organizational infrastructure to support the achievement of its vision. At last financial sustainability is a part of organizational sustainability. It has to do with the ongoing ability of the organization to generate enough resources to work towards its vision.

What makes an organization sustainable? In order to be sustainable, an organization must:

have a clear strategic direction;

be able to scan its environment or context to identify opportunities;

be able to attract, manage and retain competent staff;

have an adequate administrative and financial infrastructure;

be able to demonstrate its effectiveness and impact in order to leverage further resources;

get community support for, and involvement in its work.

What makes an organization financially sustainable? To be financially sustainable, an organization must:

have more than one source of income;

have more than one way of generating income;

do strategic, action and financial planning regularly;

have adequate financial systems;

have a good public image;

be clear about its values (value clarity);

have financial autonomy.

What is financial autonomy? Financial autonomy does not require that an organization is 100 % self-financing (financed completely from income it earns). It does require that an organization is not wholly dependent on one source for its financing. A mixture of different sources of financing is needed. But it does not exclude donor funding, or contributions from private individuals. An organization has financial autonomy when:

it is able to make its own decisions about how it generates and spends its funds;

it is able to reject "doubtable sources" of funding because such funding does not fit its values or vision;

it is able to make its own decisions about how much to pay to its staff.

There are crucial threats to financial autonomy when:

1. The organization relies on only one major donor, and the withdrawal of that donor's support will mean the failure of an organization. What happens if the donor insists on organization's payment of such low salaries that this will badly influence the quality of its performance? What happens if the donor expects the organization to follow the donor's agenda at the expense of its own one?

2. The organization relies only on foreign donors who may change their funding priorities at short notice.

3. The organization relies entirely on earned income and has to do work that generates income, irrespective of whether or not it fits with the values or vision of an organization.

4. The organization spends money in a way that is not cost efficient and cost effective, and so wastes its resources.

Taking into account the mentioned issues, the key parameters for financial strategy can be named (Fig. 10.3).

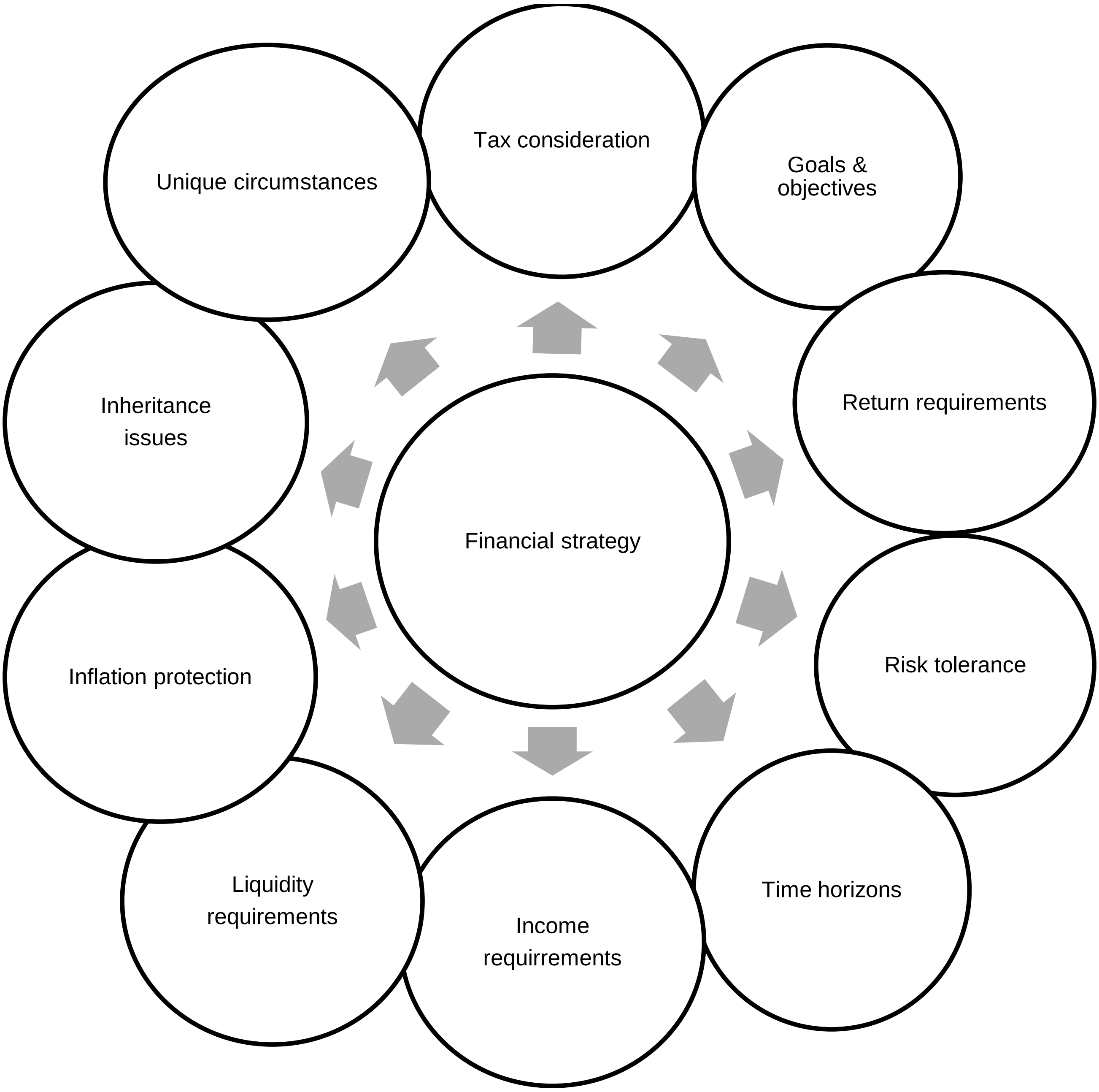

Fig. 10.3. **The key parameters for financial strategy**

A successful financing strategy requires some preliminary work. Before you develop and write up your strategy, and implement it, you need:

an organizational strategy and plan;

an organizational budget;

financial systems;

a public image and visibility;

value clarity – a clear understanding of organization values which cannot be compromised by the financing strategy.

The steps of making financial strategy are described in Fig. 10.4.

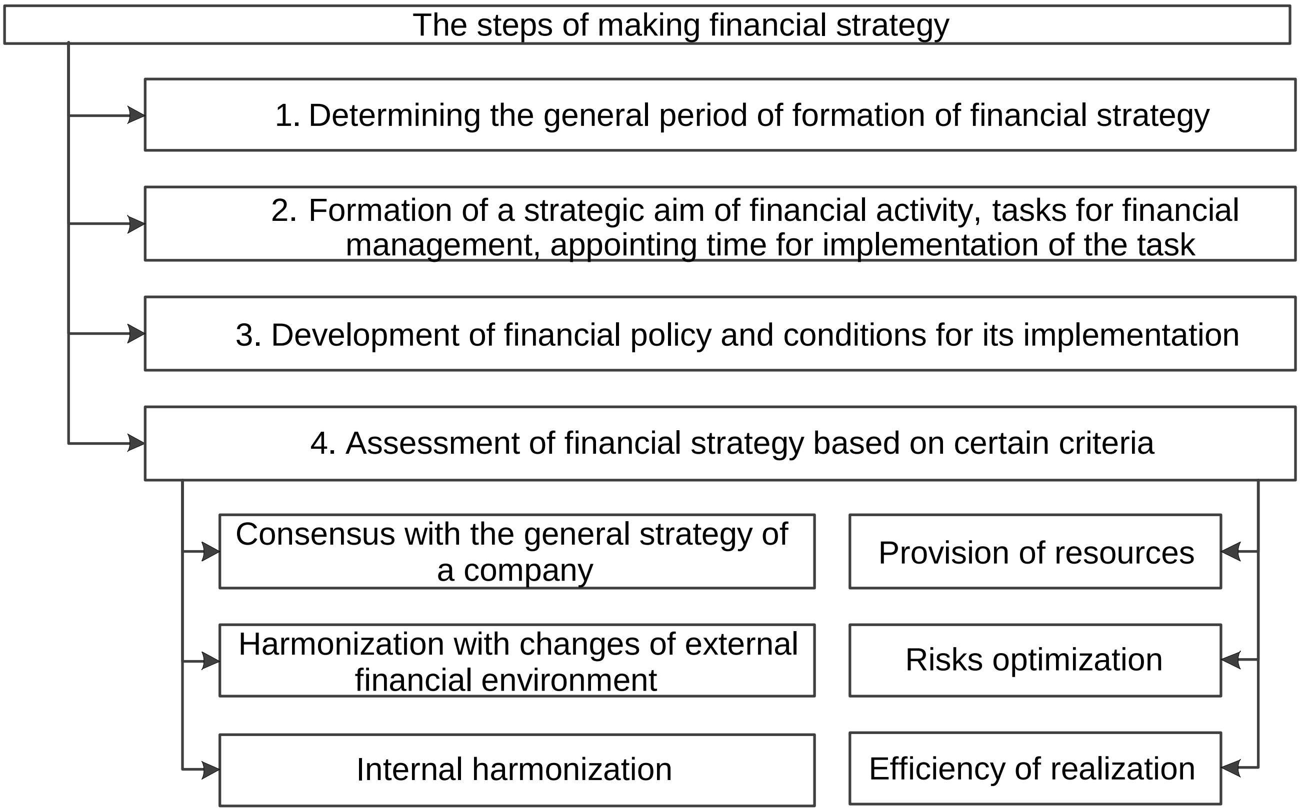

Fig. 10.4. **The steps of making financial strategy**

The achievement of strategic objectives is ensured by the formation of a system of strategic goals. The achievement of these goals, in turn, is provided by the following conditions:

making sufficient capital to form the necessary assets;

optimal structure of assets and capital;

acceptable level of financial risks of business activities;

use of financial innovations;

high profitability of using their own capital, etc.

Target indicators for the formulation of strategic financial goals are:

the average annual rate of growth of the owned financial resources;

the coefficient of profitability (return on capital) of an enterprise's own capital;

the ratio of current and noncurrent assets of a company;

the minimum level of assets which provides the liquidity of an enterprise;

the minimum ratio of the owned capital in the total capital that provides financial stability of an enterprise;

the critical level of financial risks of the enterprise economic activity;

the ratio of long-term and current liabilities, etc.

Financial policy is a set of methods of financial management for the organization and use of financial relations at an enterprise. Unlike the financial strategy in general, financial policy is formed only in specific areas of financial activity of the enterprise that requires the most efficient management to achieve the main strategic objectives.

Evaluation of the effectiveness of the developed financial strategy involves consideration of such parameters as:

harmonization of financial strategy with the general development strategy;

harmonization of financial strategy of the enterprise and changes in the external financial environment;

provision of resources for financial strategy which describes the potential and available financial resources of the enterprise to achieve strategic goals and solving the main problems of financial development;

optimization of risk levels concerning the implementation of the developed financial strategy; setting critical level of risks accepted by owners and management to provide financial balance of the enterprise;

efficiency of financial strategy realization, the definition of which is based on the estimated and actual calculations of the results of financial-economic activity of the enterprise.

Financial tactics of a company is specific financial techniques and methods used by a company to get strategic objectives.

The main task of financial tactics is to select the best solution and the most attractive tools (in a particular business situation) of financial management. Tactical aims and objectives of financial management are:

provision of reimbursement of current expenditures at the expense of the income received;

adjustment of the size of current cash payments of the enterprise;

effective use of available financial resources of the enterprise;

optimization of cash flows of the enterprise;

provision of the balance sheet liquidity;

increase of business activity of the enterprise;

strengthening the financial sustainability of the enterprise.

10.4. The financial management mechanism and its components

The mechanism of financial management is a set of key elements influencing the process of development and implementation of managerial decisions in the sphere of financial activity of an enterprise. The financial mechanism can generally be defined as a set of methods for realization of economic interests through financial impact on the socioeconomic development of the enterprise (Fig. 10.5).

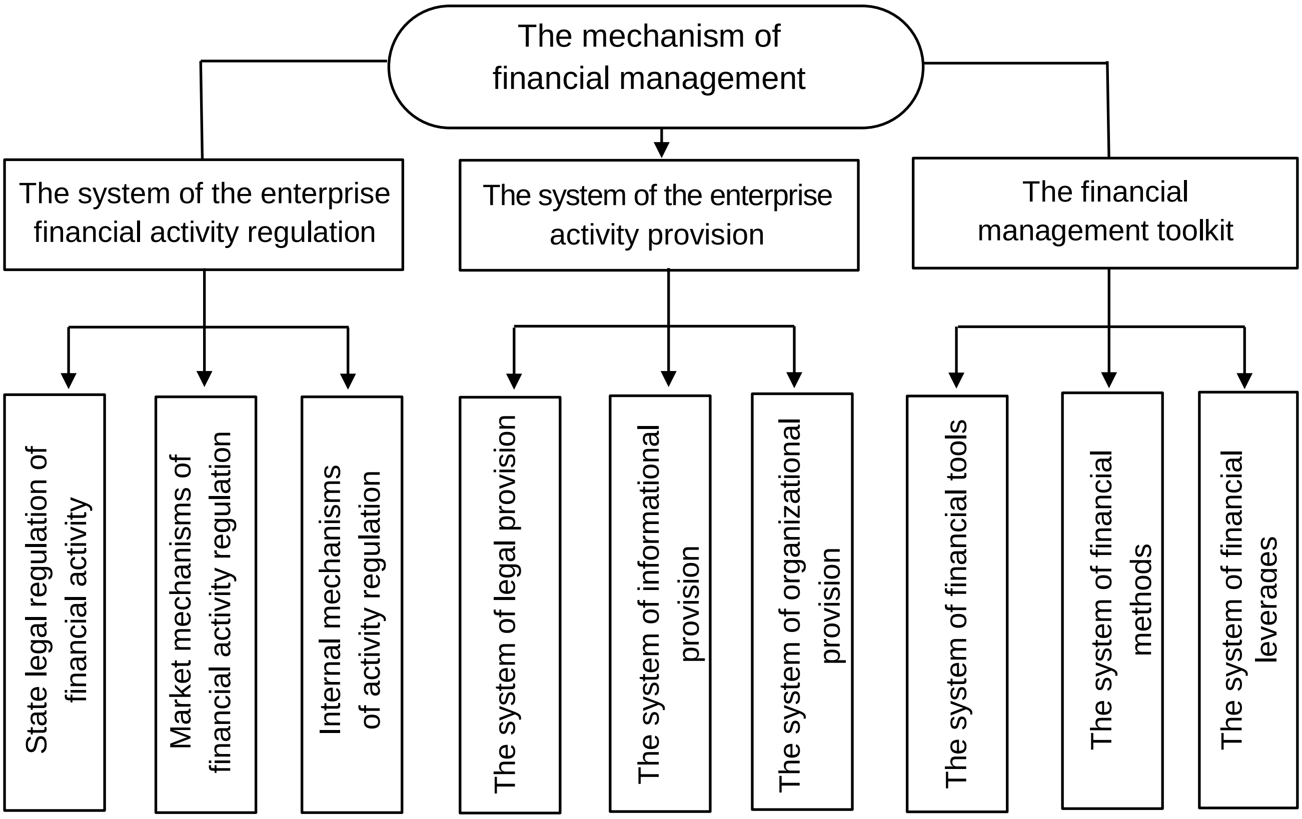

Fig. 10.5. **The structure of the financial management mechanism**

Here are some other points to include in your financial strategy.

Sensible spending. Understand how you spend your money. Prepare a household spending worksheet. It will enable you to prioritize your spending and identify areas of potential saving.

Prudent borrowing. Borrowing can enable you to obtain things that are otherwise beyond your current reach, but borrowing costs money. Loans for things that provide lasting and ongoing value (such as education, home or auto) are smarter than borrowing for short term gratification (extravagant vacations or expensive jewelry). Prudent borrowing also includes making sure that the rates and terms of your loans are as attractive as you can get. Before borrowing (whether it is a credit card, an auto loan, mortgage or any other loan), make sure you understand all the terms. The interest rate, length of loan and method of calculating interest should be clearly understood.

Consistent saving. Utilizing a payroll deduction or another automatic savings program is usually more successful than trying to save on a less regular basis. Automatic saving plans result in consistent deposits and are available in a number of forms. Select one that fits your budget and meets your long-term needs.

Wise investing. Investments come with risks, and hopefully higher returns to compensate for those risks. Understanding the risks of loss, price fluctuation and inflation are necessary when creating a sound investment strategy. Diversification, asset allocation (dividing funds into stocks, bonds and cash investments) and investment costs should all be considered as part of a wise investment strategy.

Adequate protection. Periodically, you should review all your insurance coverage. This includes homeowners/renters, health, disability, auto and any umbrella policies you may have. For peace of mind, make sure you have the right combination of coverage and deductibles. If you use insurance primarily for "catastrophic" coverage, remember that higher deductibles usually lead to lower premiums. For life insurance, evaluate how much you really need. If your family would need significant funds to replace your income, a larger policy might make sense. If you are single, perhaps a smaller policy (and smaller premiums) will be sufficient. Also, compare the benefits and costs of a term and whole life policies. For younger, healthy individuals without a need for permanent protection, a term policy may be a better choice.

Use a qualified advisor, if you need one. In areas where you need or want any help, find the right advisor. It may be an investment professional, insurance agent, financial planner, credit counselor or trusted family friend that can provide guidance. Make sure they are qualified and that you can comfortably work with them. Do your homework. The more knowledgeable you are, the better you will be able to evaluate recommendations. Remember, that your decisions will affect you and your family for a long time.

Management accountants help a business make strategic decisions by:

identifying and collecting key information;

measuring and interpreting information;

analyzing information;

communicating findings;

joining with other managers to plan changes;

monitoring, measuring and controlling progress.

For example, a business may decide to invest in a new technology to improve the efficiency of production. If it has analyzed the benefits properly, the investment will lead to growth and more profit. However, if the business has not evaluated all the factors and the technology is untested, it may not give a return on investment.

Questions for self-assessment

1. What is financial management?
2. How can financial management be connected with accountancy, production and marketing?
3. Describe the purposes of financial management.
4. What goal does financial management achieve?
5. Explain the function of a financial manager at any enterprise.
6. Explain the essence of financial sustainability and financial autonomy of an enterprise.
7. What is financial strategy?
8. What is the difference between financial strategy and tactics?
9. How can financial strategy be evaluated?
10. Name the key elements of the financial mechanism at an enterprise.

Practical tasks

Task 1. Identify the true statement concerning different ways of additional attraction of capital:

1. The cost of attracting capital is defined only by the interest rate and the terms of attraction.
2. Issuance and placement of bonds is always more preferable than issuance of shares because bonds do not give the right to participation in profit and company management.
3. A high rate of borrowed money in equity makes a company more sensitive to unfavorable changes of interest rates that can lead to company inability to serve its debt.
4. Issuance and placement of shares is always more preferable than issuance of bonds because it means attracting capital on the termless basis and does not create liabilities for debt and interest payment.

Task 2. A company sells computers at the price of 6 780 UAH. Fixed costs equal 16 000 UAH. Direct costs per computer are 4 380 UAH. It was suggested that the price be decreased by 10 % in order to be ahead of competitors. Explain how sales should change to cover price reduction.

Task 3. A company produces musical instruments, including guitars. The guitar model S-151 is very perspective and has a significant potential market. The model estimate is given below. Costs per item are: direct material costs – 10 300 UAH; direct labour resources – 9 280 UAH; general production costs – 670 UAH. Total costs are: sales costs – 7 540 UAH; administrative costs – 36 890 UAH; general economic costs – 87 800 UAH. The price of the guitar is 26 700 UAH. Define: the break-even point for this product; the operating income if the company sells 35 guitars; the operating income if the price is increased by 15 % and sales are reduced by 20 %.

Task 5. You are going to buy shares of some European machinery company. What factors will you analyze and take into account before purchasing? Define a set of key indicators which will be useful to prepare for the deal. Explain you answer.

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Розглянуто сутність та функції фінансів і фінансових відносин, грошово-кредитної системи країни, фінансової політики, державного та місцевих бюджетів, податкового регулювання економіки, особливості функціонування фінансового ринку та ринку страхування, а також механізмів регулювання фінансової діяльності суб'єктів господарювання незалежно від їхнього розміру та форми власності.

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