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## FUNCTIONING, PROBLEMS AND PROSPECTS OF HOUSEHOLDS IN UKRAINE'S FINANCIAL SYSTEM

Households as subjects of the national economy under the market conditions become crucial and, above all, the value of household finance increased in economic relations of society. Household's finance is a cornerstone of the financial system of the country's economy. They take part in defining the market, and are one of the main economic indicators of the country. Involvement in household financial cycle is seen as a prerequisite for further expansion of the domestic financial market and source of investment for the corporate sector. Households are traditionally the main supplier of investment resources, and mobilize their savings is essential for the success of financial intermediaries and, hence, one of the main factors of sustained economic growth.

However, household finances, models and strategies for economic behaviour are derived from the state loan and finance. But the global financial crisis that destroyed the financial stability of 2000-2008 was led to negative social consequences: increasing unemployment, weakening the national currency – hryvna, inflation. Ukraine came under the threat of default, rattling down the level of public confidence in the banking system, significantly reduced the real income of households.

Theory on the role and importance of households in the effective functioning of the financial system began to develop the economy in the period of classical economic theory. Category „households” was an essential element in the works of D. Ricardo, J.B. Sey, J.S. Mill, F. Edzhuorta, A. Marshall,

A. Pigou and G. Keynes. Of classical political economy and other economic schools consistently developed this category, as the segment of the financial system – from individual to national, determining its function and significance of each historical period. In mid-1960 XX century with the emergence of „new” theory, where households are presented as the main producers of vital goods, households were again seen in the works of G. Becker, K. Lancaster, D. Minser and others. Among domestic scientists in this issue should be allocated as: V. Geets, A. Chukhno, S. Panchyshyn, M. Savluk, I. Kukuru-dza, A. Archangelskiy, G. Volinsky, N. Holod<sup>1</sup>.

However, due to the effects of global financial crisis, the financial activity's of households becoming a main problem that determines the relevance of the proposed article.

Analysis of household behaviour in the light of the financial system outlined by classic cycle of financial and commodity flows in a market economy. At the same time highlight that households, firms and state-related channels in this scheme of commodity and factor markets. On the one hand, households invest in the company, buying goods and services from other households, are suppliers of labour and capital. At the same time underline that marked textbook scheme ignores the crucial component of a market economy, namely: monetary-credit market. Therefore, build analysis, taking into account the following three financial sectors like households: income, expenses and savings.

At first we must understand that the financial behaviour of households as the subjects of the financial system depends on so many factors – objective: the level of income, trends in financial institutions, money supply, inflation, exchange rate, interest rates etc. and Subjective: estimations and expectations regarding the economic prospects of the country, level of confidence in banking institutions, propensity to savings etc<sup>2</sup>. The first group of factors usual-

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<sup>1</sup> А. А р х а н г е л ь с к и й, О. Р а д з і є в с ь к и й, А. А л е к с е є в. *Бідність, податки та економічне зростання* // Економіка України. – 2006. – № 5. – С. 63-71; Г. В о л и н с ь к и й. *Про соціальну диференціацію населення* // Економіка України. – 2008. – № 2. – С. 79-84; *Доходи та заощадження в перехідній економіці України* / За ред. С. Панчишина, М. Савлука. – Львів: ЛНУ ім. І. Франка 2003. – 406 с.; І. К у к у р у д з а. *Національна стратегія підвищення якості життя / Майбутнє України: стратегія поступу: монографія.* – Донецьк: ТОВ «Юго-Восток – ЛТД 2008. – С. 33-43; Н. Х о л о д. *Розподіл доходів і бідність у перехідних економіках: монографія.* – Львів: Видавничий центр ЛНУ ім. Івана Франка 2009. – 442 с.

<sup>2</sup> *Российские домохозяйства накануне финансового кризиса: доходы и финансовое поведение.* / Отв. ред. Л.Н. Овчарова. – М.: Независимый институт социальной политики 2008. – С. 193.

ly have a basis for assessments of macroeconomic dynamics of financial behaviour. Focus attention on the second group of factors characterizing the nature of institutional approach, a model which rejects neoclassical economic behaviour of households. From the institutional point of view this model is too abstracted to real economic life is determined by perfect rationality and knowledge. In turn, institutional theory defines the behaviour of households as a complex interweaving of formal and informal institutions, where the focus is directed only in the purely quantitative characteristics, and understanding general trends in the light of transaction costs, and specification of property rights.

It should be emphasized that in all market economies are the mechanisms of redistribution of income, so decided to separate primary and available cash income households. Primary incomes of private households are formed as a result of market transactions – the sale of goods and factors of production. Accordingly, they are formed by wage employees, property income, business income, and income from self-employment. More are effective mechanisms of income redistribution. All social benefits and transfers (except those who receive in-kind) are added to the primary household income, and from the amount paid income taxes, property, social security contributions and other payments. The result remains the disposable income of households.

Analyze the situation with the disposable income of domestic households (Fig. 1). Experts believe the World Bank, the most important position is the separation of the middle class income for each household member, which is determined from 3500 to 8000 American dollars a month. This criterion corresponds to the richest countries – USA, Japan, Switzerland, UK, in other countries to the middle class include the following indexes: Germany - from 2000 American dollars, Spain, Portugal – 1000 American dollars, Greece – 750 American dollars. For poor countries, belongs to Ukraine, meets the criteria specified level of income per household member within 300-400 American dollars i.e. 2-5 subsistence minimums<sup>3</sup>. Note that in developed countries middle class is 55-60% of able-bodied citizens.

According to EU standards is the poor who receives less than 60% of the average wage in the country. Under this criterion, the lowest minimum wage in the EU receive in Bulgaria and largest – in Luxembourg.

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<sup>3</sup> С. С к и б и н а. *Дифференциация доходов домохозяйств и ее влияние на степень социальной стратификации общества* // Экономика, финансы, право. – 2009. – № 11. – С. 23-27.

As for Ukraine, according the survey results, conducted by the Kiev Institute of Control Sciences by Gorshenin (2006), Ukrainian middle class is at an early stage of development and it refers only 8.9% Ukrainian. That is, socio-economic conditions prevailing during the transformation of the domestic economy are not conducive to the formation of the middle class. Data on the distribution of households by level of average per show expenditure of money, that Ukraine was formed instead of the middle class poor class<sup>4</sup>.

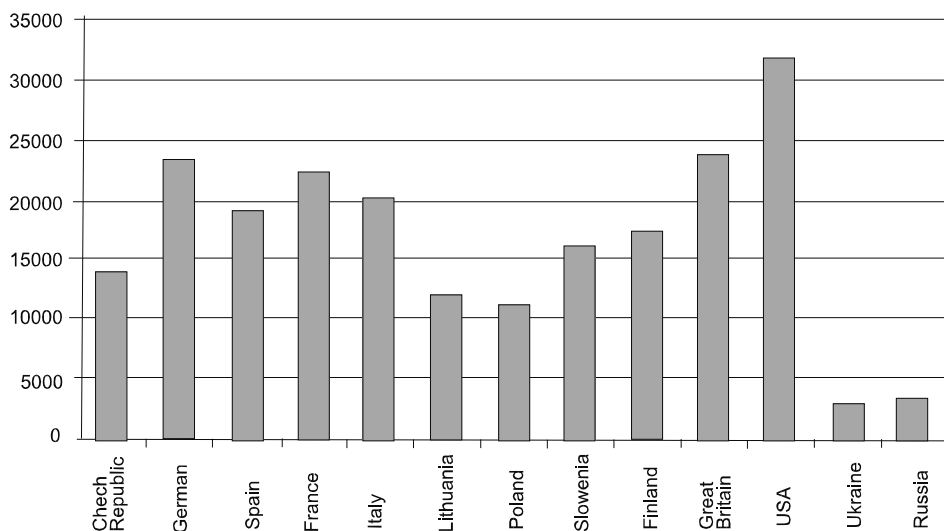


Figure 1. The incomes of households in some countries during the 2007 (the year on the eve of financial crisis) (EUR).

Sources: <http://epp.eurostat.ec.europa.eu>, <http://www.ukrstat.gov.ua/>, <http://www.gks.ru/>

You must also stress that Ukraine has a significant gap between the poles of household property, which continues to grow. However, given the undocumented income, the bulk of their property to enhance the differentiation provides 30% richest households.

<sup>4</sup> С к и б и н а. *Дифференциация доходов домохозяйств* с. 26.

Table 1. Structure of total households income in Ukraine\*

Incomes	Period	2005	2006	2007	2008	2009
Incomes, %		86,4	87,6	89	87,9	88,5
– Salaries		46,0	48,4	50,6	49,4	47,9
– Income from business and self-occupation		4,9	4,6	5,2	5,3	5,1
– Revenues from sales of agricultural products		4,6	3,8	3,6	3,3	2,9
– Pensions, scholarships, social assistance, in cash		24,0	23,7	23,0	23,1	26,0
– Financial assistance from relatives, other persons and other cash income		6,9	7,1	6,6	6,8	6,6
– The cost of the consumed products obtained from private households and from self-store		6,0	5,4	4,8	4,0	4,6
– Non-cash benefits and subsidies for housing and communal services, electricity, fuel		0,5	0,6	0,7	0,5	0,6
– Non-cash benefits to pay for goods and health services, travel services, tours of recreation, etc., for the services of transport and communication		0,6	0,6	0,5	0,5	0,6
– Other revenues		6,5	5,8	5,0	7,1	5,7
Memo: total revenue, USD.		262	319	398	376	389

\* Source: <http://www.ukrstat.gov.ua>

This conclusion includes the following information. Its domestic households meet the needs within the resources that come from different sources (Table 1). Average monthly total income of a household in the first half amounted of 2009 was 2937 hryvnas and increased compared to 2008 with 9%. At the same time emphasize that only half of total household income accounted for income from employment, whose share in the period decreased by 3%, primarily by reducing wages. However, state transfers (pensions, scholarships, social assistance) were more than a quarter of total income<sup>5</sup>. Thus we can conclude that the crisis led to the deterioration of living standards, but did not factor in the formation of structural changes in household income.

With regard to costs, they define as common household spending on consumer durable goods and services and short-term use, produced domestically and imported from abroad. In the first place – the cost of housing, food and

<sup>5</sup> Л. Ш а н г і н а, В. Ю р ч и ш и н. *Структура доходів і витрат домогосподарств «не відчула» кризи* // Макроекономічний огляд України. – 2009. – Грудень. – С. 4.

clothing is meet vital needs. Therefore, their share in total household expenditures on consumption is an important indicator of living standards.

Table 2. Total expenditure of households in some countries (eur)

Country	2008	2009
Germany	17140	17791
France	17530	19756
Italy	15660	15143
Latvia	6290	10221
Portugal	10440	11244
Slovenia	9700	12047
Slovakia	6820	10244
Finland	18050	21931
Sweden	16680	19332

\* Source: <http://epp.eurostat.ec.europa.eu>

As for Ukraine, the average monthly total costs of a household in the first half of 2009 amounted to 2680 hrivnas<sup>6</sup>. Compared with the general expenses of households in some countries (Table 2), this figure is demeaning to our country, given its socio-economic potential. The reduction in real disposable income according to the same period in 2008 influenced the changes in the structure of total costs. The most significant article (53%) remain the costs of food, purchasing food products and the services – 32% of total expenditures, significantly reduced the share of costs related to buying durable goods, as well as cost recovery and rest. At the same time as the share of total non-consumer expenditures, which amounted to only 13%, mainly due to lower costs, which were directed to savings. Thus almost 90% of total household expenditures is consumer, which in essence defines total costs as „conditioned”.

The third element of the proposed analysis, the category of savings – is part of money income, gradually formed and is available for current consumption in order to further use or obtain additional income. Costs are not consumed in the current period, acquire the three main forms: deposits in commercial banks and securities, foreign exchange savings, cash balances on

<sup>6</sup> Ш а н г і н а, Ю р ч и ш и н. *Структура доходів і витрат домогосподарств «не відчула» кризи с. 1.*

hand. At the same time emphasize that a necessary condition for economic growth is the presence of a substantial share of accumulation in the structure of the gross domestic product. Meanwhile, the overall trend of GDP in Ukraine is to reduce the share of savings.

Although in terms of financial stability and strengthening the national currency observed positive increase in commercial banks deposits population (Table 3), but with the beginning of the financial crisis and devaluation of the hryvna was back and the volumes of households buying foreign currency bank currency market exceeded sales. It rests on deposits of households in national currency reduced (in 2009 – 2,8%), and in dollars and euros increased (in the annual calculation of 4,2 and 6,4% respectively). During 2009 investors held a cautious position and place the funds in the short term, volumes continued to decline long-term deposits (deposits available from 1 to 2 years in the annual calculation amounted to minus 52.7%)<sup>7</sup>.

Table 3. Deposits of households involved in deposit corporations, except National Bank of Ukraine (balances at end of period, UAH mln.)\*

Period	2005	2006	2007	2008	2009
Total	74778	108860	167239	217860	214098
At the request	18660	25940	40123	40578	57265
Up to 1 year	19025	22853	32504	55878	98157
From 1 year and over	37093	60066	81901	98626	58676
In local currency	43688	59889	102379	110016	101081
In foreign currency	31090	48970	64860	107884	113016

\*Source: Бюлетень Національного банку України (електронне видання). – 2010. – Лютий.

The main purpose of savings was postponed demand for the purchase of durable goods. Savings grew in the present context are, basically, the forced nature (except for households with high income, representing a minority). In general, forced savings can be divided into the following two types: 1) forced insurance and 2) forced savings. The first type of savings is due to uncertainty in future population and concern about the need for an emergency reserve.

<sup>7</sup> Бюлетень Національного банку України. Щомісячне аналітично-статистичне видання НБУ. – 2009. – № 12. – С. 34.

The second type of savings – forced savings that will occur in households due to unavailability of some material benefits in the short term, with most of these benefits is necessary. Typically, these savings are liquidated and the urgency of the conditions of accumulation of necessary funds.

Regarding investment of households, it provides direct investment and direct investment in the process or the use of financial intermediaries: banks, investment funds, insurance companies, pension funds and stock exchanges.

A developed financial system is characterized by the presence of money market a significant number of financial institutions and provides an effective process of transformation of savings into investment. Unfortunately in Ukraine is still not as efficient stock market and confidence in the banking system.

Attracting money banks households is one of the main directions of monetary policy, because a significant portion of banks' resource base and a positive impact on the economy as a whole. Therefore, the work of raising household should take in politics National Bank and commercial banks' prime location, especially in the current global financial instability and sharp fluctuations in currency exchange rates. Thus, despite the sharp fall in prices of real estate market, the majority of Ukrainian households, as before the crisis, consider investing in this segment is the most reliable way of savings. The share of those who want to keep money in cash has almost doubled and the number willing to invest in deposit accounts of commercial banks and the stock market declined significantly.

So, make the following conclusions.

Ukraine over the last decade has substantial slowdown in economic development. GDP reached only 74.1% compared with 1990, since 1991, real household income declined in 1999 to 32.9%, and then increased to 101.3% in 2008<sup>8</sup>. That is, for 18 years of independence, Ukraine was almost real income growth, with the lion's share of resources concentrated in a very small number of households.

In times of crisis we have transformation steep decline in incomes and living standards of a large number of domestic households that provoked the need for greater guarantees of social protection and the simultaneous strengthening of the tax burden on entrepreneurs. That is why the share of social

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<sup>8</sup> Н. Яценко. Экономика Украины 1999-2008: потерянное десятилетие // Зеркало недели. – 2009. – № 51.



spending in total state expenditures and GDP is growing – from 17% in 1999 to 28% in 2008 .

Improving household incomes is a key problem of modern social and economic development. Now we have a significant backlog of Ukraine for this indicator from the standards of developed countries. However, wages can not be considered separate from the main macroeconomic and overall dynamic proportions. After the accession of Ukraine during a political business cycle in late 2004 was disproportionate growth of wages compared to gross profit of GDP. In 2005 due to rising wages its share in GDP increased to 49.1%.

Thus we can conclude that Ukraine is the excessive growth of wages compared to its performance, which significantly deforms macroeconomic proportions.

Therefore wage inflation should have no basis and determined by productivity and expansion, thus achieving the minimum wage to subsistence level, and then – the minimum consumer budget. Proposed measures to improve the financial position of households in Ukraine's financial system will add the need for labour outstripping wage growth compared to other household income, introducing flexible taxation policies that encourage entrepreneurship, funded pension system and restore confidence in the domestic banking system.

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#### FUNCTIONING, PROBLEMS AND PROSPECTS OF HOUSEHOLDS IN UKRAINE'S FINANCIAL SYSTEM

##### S u m m a r y

The problems of formation and development of Ukrainian households in transformation of the financial system.

**Key words:** households, household finances, expenses, income, household savings in Ukraine.

#### FUNKCJONOWANIE, PROBLEMY I PERSPEKTYWY GOSPODARSTW DOMOWYCH W SYSTEMIE FINANSOWYM UKRAINY

##### S t r e s z c z e n i e

W artykule przedstawiono problemy kształtowania i rozwoju ukraińskich gospodarstw domowych w transformacji systemu finansowego.

**Słowa kluczowe:** gospodarstwa domowe, finanse gospodarstw domowych, wydatki, przychody, oszczędności gospodarstw domowych na Ukrainie.