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Financial Leverages of Structural Changes in Transition Economy

Abstract. *Assessment of the modern structure of economy of Ukraine is given, factors, which caused existing disproportions are defined. The inevitability of structural changes in economy, which have to take place within the structural politics of the state are justified. The analysis showed that Ukrainian business entities are in a difficult financial situation, which complicates their investment activity and inhibits structural changes. This means that state incentives are needed for the progressive structural changes in the economy, including financial ones. However, state support should help increase the financial potential of economic entities in order to have a positive impact on the economy.*

Keywords: *structure of economy, structural policy, branch, investment, structural changes, financial support, financial assistance, financial potential of the enterprise*

1. Introduction

The topic of structural changes in economy is of particular interest both for Ukraine and for countries with transition economy. This is due to active reforming after 2013 for qualitative renewal of economic system, ensuring economic growth and development. System reforms are required by international collaborates, in particular the IMF and the World Bank.

Problems of structural reforming of Ukrainian economy and its financial support are highlighted in the works of well-known scholars and economists, such as V. Geyets, L. Shynkaruk [2011], V. Gusev [2011], D. Chernikov [2013] and others.

The purpose of the research is to substantiate the expediency of implementation of state active structural policy and the use of financial leverages to stimulate of progressive structural changes in economy of Ukraine.

2. Presenting main material

The economic system is a complex structural entity. The structure (from the Latin *structura* – construction, placement) is determined by the internal form of the organization of elements of the system, the set of stable relationships between its parts, ensuring its integrity, functioning and development. The structure is one of the defining characteristics of the system, the determining factor of its functioning.

The structure of the national economy is most often viewed through the prism of industries (the industry is understood as a set of enterprises grouped by the types of activity), regions, sectors, technological processes, respectively, the economic structure can be represented as a system of proportions and relationships between them.

To the peculiarities inherent in the structure of the economy, we include:

- the structure of the economy is a determining factor in its competitiveness (developed service sector, the dominance of high-tech manufacturing industries in the economy is a sign of all developed countries);

- the stability of economy depends on its structure (depending on the formed structure, the economy of the country is more or less sensitive and vulnerable to fluctuations of the world economy, its state of affairs; the more diversified the structure of the economy is, the more resistant it is to external influences);

- the external environment of activity of the business entities changes faster compared with changes in the internal environment, therefore, the structure of the economy is formed both under the influence of market factors and under the influence of the state; The state sets the vector for structural changes, based on national interests;

- the economic structure is inert, changes in the structure of the economy are of a long-term nature, therefore, should take place in the context of a defined development strategy.

The structure of the economy should guarantee the economic sovereignty of the state, its economic security, and also ensure a high level of competitiveness of national production, the active participation of national producers in the world market. If these conditions are not met, the necessary structural changes are required.

Structural changes are one of the results of economic development. Structural changes are quantitative or qualitative changes in the components and links of the

structure of the economy. The result of a change in the proportions of the structure that arises as a result of the accumulation of structural changes is a structural shift. In its turn, structural transformation is the result of consolidation of structural changes, which leads to changes in the proportions of social production. Therefore, any transformation involves the implementation of a number of structural changes in the system, which leads to changes in its functional characteristics.

Structural changes can be considered broadly and narrowly. In the narrow sense, these are changes in the product-sector structure of the economy. In the broad sense, these changes should be accompanied by changes in the composition of production and consumption of resources: investment and fixed capital, labor, material and energy resources [Shynkaruk 2011].

Changes in the structure of the economy can be both positive and negative, causing the modernization or degradation of the economy. Structural changes can be expressed by different economic characteristics – the number and qualification of workers, volume of production, size of capital and investments. Consequently, structural changes concern not only the quantitative proportions between sectors and branches of the economy, but also their qualitative content – the range of products, technologies used, qualifications of employees, organizational and economic forms of enterprises, etc.

Structural changes and their most significant manifestations, such as structural changes, have a decisive influence on the formation of further trends of economic development. An economy dominated by high-tech industries requires highly skilled workers, education and science, respectively, and there is a demand for interesting and creative ideas.

The structure of the economy includes a set of business entities that arose on the basis of the social division of labor, natural resources, historical traditions and territorial specificity. We consider the indicators that characterize the structure of the Ukrainian economy and give an estimate of structural changes.

Under favorable starting conditions, for 28 years Ukraine shows a lagging up to 25 times in comparison with EU countries according to the indicator of gross national income per capita. For example, GDP per capita in Poland in 2017 amounted to about 29,6 thousand dollars in terms of the parity of purchasing power, and in Ukraine these figure amounted to 8.8 thousand dollars in accordance.

The root cause of the failure of the Ukrainian economy is that its structure has not been systematically upgraded since the times of the USSR. Scientists point out that the structure of Ukraine's economy is characterized by "weak innovation, progressive primitization, a significant reduction of self-reproduction opportunities on an effective basis" [Shynkaruk 2011].

When we compare the structure of economy in Ukraine and the most developed countries in terms of three sectors we see, that the service sector, which characterizes the post-industrial economy, is dominant in all countries. For a more

in-depth analysis, it is worth analysing the service sector, highlighting its sub-sectors. The sector of agriculture is significant in Ukraine, and the industry dominates in the G7.

The basis of the Ukrainian economy is traditionally agriculture, relatively well-developed industry (food, metallurgical, coal, machine- and shipbuilding), as well as the rapidly evolving service sector.

The generally accepted macroeconomic indicator, reflecting both the volume of national wealth and its structure, is gross value added (GVA). The structure of gross value added is shown in Table 1.

Table 1. The structure of Gross Value Added in Ukraine by types of economic activity (%)

Type of economic activity	2010	2014	2018
Agriculture, forestry and fishery	8.4	11.7	13.8
Industry	25.7	23.4	20.1
Construction	3.7	2.7	2.3
Wholesale and retail trade; transport; temporary placement and organization of food	25.8	24.9	24.3
Information and telecommunications	3.5	3.8	4.4
Financial and insurance activities	6.4	5.1	3.2
Real estate activities	6.1	7.2	7.2
Professional, scientific and technical activities; administrative and support services activities	4.1	4.7	4.9
Public administration and defence; education; healthcare and social assistance	14.8	14.6	15.1
Other services	1.5	1.9	0.8

Source: State Statistics Service of Ukraine, <http://www.ukrstat.gov.ua/> [accessed: 15.09.2019].

Unfortunately, there is a tendency to reduce the contribution of industry to the creation of value added with the simultaneous growth of the contribution of agriculture. The sphere of trade, transport services, temporary placement and organization of food generates a quarter of value added in the economy. At the same time, total financial and insurance activities, information and telecommunications sectors account for less than 10% of gross value added.

The average rate of innovative enterprises is 15.6% in 2018. Pprocessing industry prevails in the volume of industrial products; the share of extractive industry remains large – more than 10%. By volume of sales, the leader is the food industry, which has quite high profitability indicators. Significant is the share of metallurgy, the enterprises of which are large exporters. We negatively assess the decline in the share of sales of machinery in the volume of sales, as well as the decrease in profitability of machine-building enterprises.

Table 2 lists the enterprises by type of economic activity (excluding banks).

Table 2. Indicators of Ukrainian enterprises by types of economic activity

Types of economic activity	The level of profitability (loss) of all activities		Enterprises that have suffered losses (%)		Share of equity in the liabilities (%)		Retained earnings (uncovered loss)		Share of short-term bank loans in liabilities (%)	
	2012	2018	2012	2018	2012	2018	2012	2018	2012	2018
Total	0.5	4.5	42.7	41.0	35.2	24.68	57.0	433	6.2	5.43
Agriculture, forestry, fishery	16.3	13.0	30.8	10.8	53.6	47.86	80.2	67	5.7	5.14
Industry	0.8	3.3	43.0	43.6	38.7	17.48	37.2	156	4.5	7.39
Construction	-4.2	1.1	46.1	45.6	11.3	-5.43	-18.2	5.6	4.0	3.53
Wholesale and retail trade	1.7	11.8	39.7	35.4	9.6	1.32	-5.5	88.1	10.8	7.64
Transportation	0.7	-4.0	47.2	46.9	50.7	61.15	12.2	-20.7	3.7	0.72
Temporary placement and nutrition	-3.8	5.7	43.6	44.9	36.4	-6.89	-5.6	2.8	2.6	4.11
Information and telecommunications	2.7	8.4	43.1	43.6	40.0	19.06	-7.0	18	5.0	4.51
Financial and insurance activities	4.2	14.5	43.2	43.1	54.0	35.18	30.7	85.6	3.0	2.41
Professional, scientific and technical activities	-8.6	0.3	44.0	48.5	34.9	-4.07	8.5	0.8	8.5	4.09

Source: State Statistics Service of Ukraine, <http://www.ukrstat.gov.ua/> without banks [accessed: 15.09.2019].

The analysis of financial results, the ratio between equity and loan capital of enterprises, suggests that most of them are in a financial crisis. Over the past few years, the activity of key industries for the industrial revival – extractive industry, metallurgical, chemical, food, mechanical engineering, and energy has been unprofitable. In such a situation, enterprises do not have an internal development potential.

In general, profits of profitable enterprises (in 2018 they accounted for UAH 746.0 billion) were bigger than losses of unprofitable enterprises (in 2018 they accounted for UAH 313 billion). In 2015 we had the opposite picture – losses were bigger than profits. The share of unprofitable enterprises exceeds 26% of their total number. Negative financial results testify to the inability of producers to cover their expenses by their own revenues. This is a factor in their additional capitalization; it deprives investment resources, redirects management to survival, not development.

In the face of a lack of revenue, enterprises are increasing their debts. At the same time, the share of bank loans in liabilities is low, due to the high cost of credit resources – rates on bank loans hugely exceed the profitability of industrial activity.

The industry is locked on its own funds as a source of investment in development, but this source is also limited, given that its own funds in the industry amounted to about 20%. In the structure of sources of investment, the share of borrowed funds, funds of foreign investors, population, investment institutions, funds of the state and local budgets decreases. The lack of funds and the inability to attract financial market resources for investment doomed manufacturers to further loss of technological competitiveness. In general, the lack of capital in the manufacturing sector remains a serious obstacle to the industrial recovery of the country's economy.

Not the best situation is with financial results and in small business. Analysis of the results of financial activity for 2015-2018 showed that among small business 68.6% were profitable, and 31.4% were loss-making.

Consequently, we can conclude that progressive structural changes in Ukraine are impossible without an active state structural policy.

Active structural transformations require adequate financial support. As we know, structural changes are accompanied by the movement of capital – more profitable and promising industries are flowing from the sectors of less profitable and unpredictable financial resources. In this case, the benchmark for investment is the market factor – the rate of profit.

At the same time, this is the task of the state to determine the prospects of one or another type of activity, its expected profitability in view of existing trends. It is the state which seeks to keep track of global trends, shape economic strategy and transform them into structural and investment policy decisions, contributing to this positive structural change.

For example, the determinants of growth in a post-industrial information economy are the level of development of high-tech industries and the potential of human capital. It has already been recognized that deep structural changes in the types of economic activity taking place in most developed countries will destroy sectors and professions in the near future, especially those that do not require high qualifications. Accordingly, it makes no sense to provide support to the industries of low technological processes. The state should stimulate investment in science and education, and financially support those enterprises that carry out innovative activities.

During 2014-2018, Ukrainian government officials adopted a series of legislative acts and strategies aimed at improving the fiscal and regulatory environment in order to stimulate investment, which could lead to positive structural changes. In particular, these legislative acts provide exemptions from VAT and

corporate income tax for certain sectors and territories of priority development, as well as for economic entities participating in industrial and technological parks.

In developed countries, the state took an active position in stimulating progressive structural changes [Pasinovych, Sych 2018]. Thus, in most countries, they have taken a course on active industrialization with a new technological way, with the focus of industrial policy being knowledge economy. Industrial policy is one of seven major initiatives in the context of Europe 2020 strategy launched in 2010. The European Commission (EC) stated in 2012: “The political focus on industry is based on the awareness that a strong production base is essential for a rich And an Economically Successful Europe.”

The process of reforming state aid to business entities has been carried out by many European countries that have been integrated into the European Union. It is based on the idea that in the presence of a common European market, common rules are needed for companies to ensure they have a level playing field. The EU mainly uses horizontal state aid, which includes measures to support a wide range of enterprises in order to achieve goals that are important for the whole of society, and not for individual sectors of the economy. An example of horizontal measures is the support of small and medium-sized enterprises, regional development, research and development, employment, etc.

Instead, vertical (sectoral) assistance prevails in Ukraine. The Government of Ukraine can provide support to certain types of economic activities in order to ensure the viability and competitiveness of domestic producers, in particular, in the strategic sectors of the national economy. The list of grounds for such support is defined in Article 16 of the Commercial Code of Ukraine.

The term “state support” covers any form of state support for business entities, including state aid. State support aimed at promoting the development of certain priority sectors or certain types of economic activity, including measures to preserve and support the national heritage, culture and sport, is classified as “sectoral” support.

It has to be noted that the provision of state aid to economic entities in Ukraine is non-transparent, information on its provision is not published on a single resource, and statistics on volumes are not generalized by any agency.

As a rule, Ukrainian governments provided direct financial assistance in the form of subsidies and grants to certain sectors (sectoral assistance). In 2014, according to the Ministry of Finance of Ukraine, direct subsidies to the Ukrainian economy amounted to 2.8% of GDP, and in 2013 to 3.3% of GDP.

Selective subsidization has the most negative impact on competition, since it directly reduces the running costs of enterprises, thereby creating unequal conditions for their operation, and does not stimulate enterprises to invest in efficiency. In addition to subsidies, in various years there were tax breaks for enterprises in

the mining and smelting complex, shipbuilding, aircraft engineering, automotive, light industry, chemistry, and energy.

A study conducted by authoritative scholars has made it possible to state that “the influence of state support on the level of competition, trade and the efficiency of spending public funds in Ukraine is practically not controlled. Similarly, little attention is paid to the study of state needs, the analysis of the feasibility and proportionality of any type of direct or indirect state support of economic entities” [Höllzler, Libanova, Efimenko et al. 2015].

Ukraine became aware of the need to change the forms of state support, increase control over the use of public funds, as well as the effectiveness of their use. In August 2017, the Law of Ukraine “On State Assistance to Business Entities” (hereinafter – the Law), adopted in July 2014, come into force. It is positive that this Law establishes the legal basis for implementation of the system of control over state aid to economic entities.

During the transitional phase envisaged by the Law (2014-2017), all relevant public authorities should have a clear understanding of the criteria under which support for business entities can be considered as state aid.

The membership of a measure to support business entities in the category of state aid is determined solely on the basis of an appropriate assessment conducted in accordance with the Law and the decision of the official decision of the Antimonopoly Committee of Ukraine.

Article 1 of the Law of Ukraine “On State Aid to Business Entities” defines state aid as follows: “state aid to economic entities (hereinafter – state aid) is a support in any form of economic entities at the expense of state resources or local resources, distorting or threatening distortions of economic competition, creating preferences for the production of certain types of goods or the conduct of certain types of economic activity.” The Law also provides for “individual state assistance.”

State aid consists in the transfer of state resources or local resources to individual economic entities, as well as to the loss of revenue of the respective budgets.

Article 4 of the above-mentioned Law defines the following forms of state aid:

- 1) grant of subsidies and grants;
- 2) grant of subsidies;
- 3) granting of tax privileges, deferrals or instalments of payment of taxes, fees or other obligatory payments;
- 4) write-off of debts, including debt for the provided public services, write-off of penalties, compensation of losses to economic entities;
- 5) provision of guarantees, loans on preferential terms, servicing of loans at preferential tariffs;

6) reduction of financial obligations of economic entities to funds of compulsory state social insurance;

7) the provision, directly or indirectly, to economic entities of goods or services at prices below the market or the purchase of goods or services of economic entities at prices above market;

8) sale of state property at prices below market;

9) increase of the state share in the authorized capital of economic entities or increase of the value of the state share on conditions unacceptable for private investors.

As we see, the vast majority of state aid forms are of a financial nature. The stimulation by the state of progressive structural changes through the use of financial leverage should affect the financial potential of industry enterprises and the industry as a whole. Realization of financial potential by economic entities will promote positive structural changes.

T. Paientko gives the following determination to the financial potential: "This is a set of financial resources aimed at the implementation and increase of economic potential in order to maximize profits" [Paientko 2009].

Since financial elements constitute financial resources, it is primarily determined by the ability of the entity to form an amount of financial resources sufficient to finance operating activities and development. The ability to attract financial resources in the transit economy depends to a large extent on the state and is characterized by availability, alternatives, cost, and risk.

Considering the financial potential of the industry in the resource approach, we will define it as the volume of own, borrowed and attracted financial resources of its enterprises, which they can dispose for operating and investment expenses. In order for these resources to have an impact on the structure of the economy, they should not only serve the production and economic activities and improve the performance of the enterprise, but also be involved in financing investment and innovation projects and other strategic directions of the enterprise development in order to ensure sustainable and balanced development.

3. Conclusions

Consequently, the state must implement structural policy in the context of the established development strategy for progressive structural changes in the economy. In spite of the fact that developed countries prefer the horizontal support of business entities, the vast majority of business entities are in a difficult financial situation in Ukraine, which makes it impossible to develop them. Accordingly, the state should stimulate, including financial levers (in direct and indirect forms) strategically important branches. At the present stage of development, the need to

modernize the state aid system according to the criteria defined by the goals and objectives of European integration has matured. State aid should help to increase the financial potential of the industry.

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Dźwignie finansowe zmian strukturalnych w gospodarce w okresie przejściowym

Streszczenie. *W artykule przedstawiono ocenę nowoczesnej struktury gospodarki Ukrainy i czynniki, które wywołują jej dysproporcje. Konieczne zmiany strukturalne w gospodarce, będące efektem polityki strukturalnej państwa, są w pełni uzasadnione. Analiza wykazała, że ukraińskie podmioty gospodarcze znajdują się w trudnej sytuacji finansowej, co utrudnia inwestycje i hamuje zmiany strukturalne. Oznacza to, że potrzebne są zachęty państwowe, aby możliwe było przeprowadzenie takich zmian w gospodarce i finansach. Wsparcie państwa powinno przyczynić się do zwiększenia potencjału finansowego podmiotów gospodarczych w celu wywarcia pozytywnego wpływu na gospodarkę.*

Słowa kluczowe: *struktura gospodarki, polityka strukturalna, branża, inwestycje, zmiany strukturalne, wsparcie finansowe, pomoc finansowa, potencjał finansowy przedsiębiorstwa*