

Isaieva Olena, postgraduate student

*Ukrainian Academy of Banking of the National Bank of Ukraine, Sumy*

**An investigation of the quality of financial market regulation of Ukraine**

**Summary.** The value of high-quality regulatory governance for the financial market stability is probed in the article. The method of calculation the index of regulatory management quality at financial market is probed and its practical calculation for Ukrainian conditions is done.

**Keywords:** government, financial market, regulation, regulatory governance quality, index.

**I. Introduction.** Current research in the financial system and financial markets are increasingly recognizing the importance of high-quality governance in general and in particular by the supervisory authorities of the financial market. The growing attention is spared to the standards of the financial system, developed by international bodies, elements of the effective adjusting and supervision of particular branches. The different aspects of influence of government control and its quality on financial stability were investigated by prominent western economists: Das, Quintyn, Chenard [1], Čihak, Tieman [2], Mendonca, Galvao, Loures [3], Matskevich, Misonh, Malinowska-Misonh [4] and many others. However, most studies are related to the operation of certain segments of the financial markets or banking system, and there is no comprehensive approach to the analysis of the state of financial market regulatory governance in the country. Therefore, it is necessary to study the impact of regulatory governance quality on financial stability and to develop the method of calculating the index of regulatory governance quality for financial markets.

**II. Raising of task.** The primary purpose of research is to study the impact of regulatory governance quality on the stability of financial market, to develop a method of calculating the index of regulatory governance quality for financial markets, to make its practical calculations for the market of Ukraine.

**III. Results.** The first systematic approach to defining the role of regulatory governance for financial stability and assessing its condition was developed by Das and Quintyn. Their works were dedicated to the basics of regulatory governance, establishing the “governance nexus” to underline the importance of financial system governance for the effective functioning of the nonfinancial sector, and assessment the current practices with regard to the quality of regulatory governance, based on the work undertaken by the IMF and World Bank in the context of the Financial Sector Assessment Program.

A multivariate cross-sectional analysis, made by western scientists, shows that the quality of regulatory governance indeed matters for the soundness of the banking system. This was proved, using a range of control variables of macroeconomic environment, the structure of the financial system, and the political and institutional setting. The latter has a both direct and indirect impact on financial system soundness, with the indirect links showing that the effects of proper regulatory governance are amplified when supported by good governance practices in the public sector as a whole [4].

Both financial stability and high-quality regulatory governance are desirable, but at the same time difficult to formalize and quantitative measure. Based on a broad definition of public sector management proposed by Kaufman and others, good regulatory governance can be defined as: firstly, the ability to manage resources effectively and to develop, implement and provide a balanced policy of prudential norms and rules – should be seen as an obligation to comply with the delegated task, and secondly, recognition and submission of the regulatory body to more general goals and policies of the elected government of the country [1].

As supervisors in the financial sector have the exclusive tools (sanctions and restrictions of activities until the withdrawal of licenses), to prevent the abuse of these powers, while maintaining the integrity of the control functions is a key task that must be achieved through quality management [3].

The prerequisite for effective governance is strong institutional basis. Researchers Das and Quintyn identified four components that form the basis of the

high-quality regulatory governance: independence, accountability, transparency and integrity. Components interact and reinforce each other at different levels to support good governance. Constructing the index of regulatory governance quality is based on this structure. The index for country is calculated as the weighted combination of country accordance to four components, described higher, got from estimations.

Being based on the research of scientists Das and Quintyn about the impact of regulatory governance quality on the financial stability of the banking sector, we propose to evaluate the quality of regulatory governance of the financial market of Ukraine, expanding the list of standards, rules and principles developed by international organizations [1].

The key standards for financial market, that provide information to construct an index of regulatory governance quality, are the following:

- IOSCO Objectives and principles of securities regulation;
- G30's recommendations for standards and procedures at securities markets;
- General principles of protection consumers of financial services OECD;
- Core principles for effective banking supervision of Basel committee;
- Code of good practices on transparency in monetary and financial policies IMF;
- Core principles of insurance regulation IAIS.

The index of regulatory governance quality (RGI) of country's financial market will be calculated as a weighted average of the ratings of full observance of key international standards, rules and principles at the financial market. This provides estimation comprehensiveness of transparency of responsibility and integrity aspects, in addition to transparency directly.

RGI for a particular country has the following kind:

$$RGI = \frac{1}{n} \left( \sum_{j=1}^n SCORE_j \right)$$
$$j = [1, n]$$

where n – number of standards used for the index;

j – specific set of standards;

SCORE – assessment of compliance with each standard, using the following weighting scheme:

$$SCORE_j = [0 \cdot nc_j + 0,33 \cdot pc_j + 0,66 \cdot bc_j + fc_j] \cdot 100$$

where for each standard the degree of compliance by country is defined as:

1=nc(noncompliance);

2=pc(partial compliance);

3=bc(broad compliance);

4=fc(full compliance);

9=not applicable/not answered.

Only valuable estimates are taken into account (the points on which the country has no data are not included in the list used of the evaluation) [1]. The higher level of index and its growth dynamics are desirable.

The Table 1 shows the results of the author's assessment of the implementation international standards and regulations of financial market in Ukraine. This study actually formed the initial basis for calculating the index of regulatory governance of Ukrainian financial market.

Table 1 – Results of the author's assessment of the implementation of international standards and regulations of financial market in Ukraine

Standards, principles, rules, guidelines		Years					
		2006	2007	2008	2009	2010	2011
IOSCO Objectives and principles of securities regulation	full compliance	22	22	22	22	22	25
	broad compliance	9	9	12	12	12	9
	partial compliance	5	6	3	3	3	4
	noncompliance	2	1	1	1	1	0
G30's recommendations for standards and procedures at securities markets	full compliance	1	1	1	1	2	2
	broad compliance	0	0	0	0	0	0
	partial compliance	4	4	4	4	3	3
	noncompliance	4	4	4	4	4	4
General principles of	full compliance	1	1	1	1	1	1

protection consumers of financial services OECD	broad compliance	4	4	4	4	5	6
	partial compliance	5	5	5	5	4	3
	noncompliance	0	0	0	0	0	0
Core principles for effective banking supervision of Basel committee	full compliance	10	10	10	12	12	12
	broad compliance	4	5	6	5	5	5
	partial compliance	10	9	8	7	8	8
	noncompliance	1	1	1	1	0	0
Code of good practices on transparency in monetary and financial policies IMF	full compliance	43	44	44	44	45	48
	broad compliance	12	11	11	13	13	10
	partial compliance	9	9	9	7	7	7
	noncompliance	12	12	12	12	11	11
Core principles of insurance regulation IAIS	full compliance	1	2	2	2	2	3
	broad compliance	6	5	5	5	5	4
	partial compliance	1	1	1	1	1	1
	noncompliance	0	0	0	0	0	0

As a result of calculations, carried out by us on the basis of information of table 1, we obtained the values, given in Table 2.

Table 2 – The indicators of performance of the basic requirements to financial market functioning of international organizations in Ukraine

Indicators	Years						Deviation 2011 to 2006
	2006	2007	2008	2009	2010	2011	
Indicator of implementation IOSCO Objectives and principles of securities regulation	77,87	78,74	81,34	81,34	81,34	84,89	7,02
Indicator of implementation G30's recommendations for standards and procedures at securities markets	25,78	25,78	25,78	25,78	33,22	33,22	7,44
Indicator of implementation General principles of protection consumers of financial services OECD	52,90	52,90	52,90	52,90	56,20	59,50	6,60
Indicator of implementation Core principles for effective banking supervision of Basel committee	63,76	65,08	66,40	70,44	71,76	71,76	8,04
Indicator of implementation Code of good practices on transparency in monetary and financial policies IMF	70,91	71,36	71,36	72,22	73,54	74,88	3,97
Indicator of implementation Core principles of insurance regulation IAIS	66,13	70,38	70,38	70,38	70,38	74,63	8,50
The average indicator of regulatory governance of financial market	67,66	68,47	69,27	70,27	71,67	73,51	5,85

During the period 2006-2011 the general RGI of Ukrainian financial market increased. Thus, in 2006 it was 67.66, in 2011 – 73.51, what undoubtedly positively characterizes the activities of government regulation and the state of market governance. However, there are very significant differences in the levels of performance of standards, rules and guidelines developed by different international organizations.

The best performed are IOSCO Objectives and principles of securities regulation. Also very high levels of performance is observed with Code of good practices on transparency in monetary and financial policies IMF, Core principles of insurance regulation IAIS, Core principles for effective banking supervision of Basel committee. At the same time, very low values are showed by G30's recommendations for standards and procedures at securities markets. Although all groups of indexes showed the positive dynamics of change, consequently, there has been improvement in their implementation at the Ukrainian market. And accordingly, regulatory governance at the financial market of Ukraine became more qualitative.

**IV. Conclusions.** Better regulatory governance structure enhances the stability of the financial market. Our results indicate that the impact of regulatory governance on financial stability is stronger, when country has the higher the quality of economic management in general. There is an increase of implementation level of international standards of financial market functioning in Ukraine the last years, especially IOSCO Objectives and principles of securities regulation. The offered calculation method of index of regulatory governance quality can be used in practice for taking management decisions about financial market regulation on its basis.

### **Literature**

1. Das, U. S. Does Regulatory Governance Matter for Financial System Stability? An Empirical Analysis / Udaibir S. Das, Marc Quintyn, Kina Chenard / IMF Working Paper WP/04/89. – 2004.
2. Cihak, M. Quality of Financial Sector Regulation and Supervision Around the World / Martin Čihak and Alexander Tieman / IMF Working Paper WP/08/190. –

2008.

3. Ferreira de Mendonca, H. Financial regulation and transparency of information: evidence from banking industry / Helder Ferreira de Mendonca, Delio Jose Cordeiro Galvao, Renato Falci Villela Loures // Journal of Economic Studies. – 2012. – vol. 39, №4. – P. 380-397.

4. Mackevich, M. International standards of openness and transparency of public finances in legislation and practice of Ukraine. Attempt of estimation / Marta Mackevich, El'zhibeta Malinovska-Miseng, Voycekh Miseng and others. – Warsaw, 2003. – 46 p.

5. Core principles for effective banking supervision of Basel committee (Basel Core principles) / Basel committee of banking supervision, Bank of international settlements. – Basel, 2006.

Isaieva, O. V. An investigation of the quality of financial market regulation of Ukraine [Text] / O. V. Isaieva // Nauka i studia. – Przemysl : Sp. x o. o. "Nauka i studia". – 2013. – №14. – P. 25-30.