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THE ROLE OF INSURANCE IN THE DEVELOPMENT OF THE FINANCIAL SECTOR

Summary

The study examines trends in the financial sector of the Republic of Belarus and determines the role of insurance in its stabilization. An analysis of the current state of the insurance market is carried out and the problems are identified in the article. The factors which influence the level of consumption of insurance services are represented in the article. The development of insurance protection has been analyzed through the introduction of additional obligatory insurance types. The mechanism is developed within the framework of the Strategy for the Belarusian insurance market development. The scientific novelty and significance of the obtained results lies in the methodological justification for the formation of an effective organizational and economic insurance mechanism within the functioning financial system framework of the Republic of Belarus. The essence and novelty of the proposal lies in the development of a structural and logical functional model of the insurance market with the use of a reinsurance pool in which the subjects are identified and their participation in reinsurance operations is determined. The scientific novelty includes the creation of an operating costs fund, which complies with European insurance legislation.

Key words: insurance, reinsurance, insurance market, premiums, insurance policy, risks

JEL: G11, G22, H50

1. Introduction

The financial system is an important part of the state and serves as a financial stabilizer designed to ensure sustainable economic development. A special role is attributed to the subjects of the financial sector, which must be sustainable. As economic relations develop, the financial sector strengthens and expands, financial institutions develop, and financial instruments are improved. There is a geographical correlation which provides the expansion of financial markets. The key players in the financial sector are the central bank, banks, non-bank financial institutions, insurance companies and stock ex-

changes, financial investment institutions, pension funds, credit unions, and associations.

As an intermediary, the financial sector plays a special role in the distribution of resources between all other sectors. It also functions as a cash center and provides, through financial instruments, the ability of borrowers to access all financial resources. Therefore, at the state level, there should be an impact on the regulation of the financial sector through timely changes, taking into account the ongoing integration processes, the legislative and regulatory framework, and the implementation process.

Thus, the main function of the financial sector of the economy is to maintain macroeconomic stability, plan the state budget, maintain a stable national currency, and preserve gold and foreign exchange reserves for at least a five-year cycle. In addition, a special role is assigned to transactions within the financial sector. The possibility to maintain the functions of lending from the banking sector and ensure the transmission of this support to the real sector of economy remains a very important issue.

However, the implementation of these functions can be achieved if all the elements of the financial sector function effectively.

Therefore, it is necessary to conduct a study on the theoretical justification and development of an effective organizational and economic mechanism for insurance activities. The new approaches to insurance companies function as a factor in stabilizing the financial market and the rationale for the proposals are required to be represented strictly within the framework of the financial system.

2. Specifics of the financial sector development in the Republic of Belarus

The development of the financial sector in the Republic of Belarus is paid great attention to at the state level. There are different approaches to the definition of the financial sector in the economy. From the point of view of extensive economic institutional analysis, the financial sector is a part of the economy associated with the activities of financial institutions or intermediaries. We will consider the financial sector as a set of institutions, tools, and legislative framework that ensure the effective functioning of the production process. It is necessary to mobilize temporarily free cash resources of individuals and legal entities for the normal development of the economy, and their distribution and redistribution on a commercial basis between different sectors of the economy.

The main component of the financial sector and the most important tool for socio-economic macro regulation is the state budget. The state budget is the financial program of state activity, reflecting all of its monetary resources (revenues) and their distribution (expenses). The state budget is, therefore,

the largest macroeconomic monetary fund that the government of the country uses to finance its activities.

The financial sector's effectiveness as a whole depends on each entity's effectiveness. The following institutions are parts of the financial market in the Republic of Belarus: National Bank; Ministry of Finance; banks and non-banking financial institutions; open joint stock company "Development Bank of the Republic of Belarus"; professional participants of the securities market, including the open joint-stock company "Belarusian Currency and Stock Exchange"; insurance companies, including the republican unitary enterprise "Belarusian National Reinsurance Organization", which carries out insurance activities solely in the field of reinsurance; the companies that carry out leasing activities; microfinance organizations; forex companies; other companies that carry out intermediary activities on the financial market.

There is not enough room for a cost-effective and reliable placement of financial resources available to the entities. Lending to the enterprises, with the exception of those controlled by the significant banks, involves very high risks. The absence of a well-established deposit insurance mechanism does not contribute to the growth of private deposits in the banking system.

At the same time, there is a steady growth in the main cost parameters of the banking system – capital, the volume of raised funds, including public funds in the national currency, and lending to the real sector of the economy. Dependence on public finances in the banking sector has decreased and the role of financial flows within the private sector has increased.

Therefore, as a priority direction in the medium term in the Strategy for the Development of the Financial Market of the Republic of Belarus until 2020 is the formation of a regional and global financial services market. This priority will be envisaged by the intensification of competition under the influence of technology and telecommunications, and the growing trend towards the formation of transnational financial groups; increased competition in the banking sector with financial intermediaries; active implementation of modern information technologies [*The strategy of development of the financial market...*].

Thus, the formation of a full-fledged financial market is an indispensable condition for financial stability and sustainable economic growth. However, it is necessary to observe the proportion between achieving stable high rates of economic growth and accelerating the restructuring of the economy, economic regulation with increasing living standards, using a preferential tax regime to increase economic potential and develop targeted sectors of the economy.

3. The insurance sector as part of the financial system

As a part of the financial system, the insurance sector is important for the entire economy. The insurance mechanism compensates a significant share of

losses caused by fires, natural disasters, man-made disasters and other accidental events of an unfavorable nature. Thus, insurance performs the function of re-financing, which could increase the expenditure part of the budget. In this particular aspect, in economically developed countries, insurance companies are the largest investors.

As of January 1, 2018, the insurance sector of the Republic of Belarus includes 21 insurance companies, including 4 companies that carry out types of insurance related to life insurance. The Republican Unitary Enterprise “Belarusian National Reinsurance Organization” has been operating on the national insurance market since 2006 in accordance with Resolution No. 1463 of the Council of Ministers of the Republic of Belarus of November 4, 2006. The main target of this organization is the provision of specific insurance activities exclusively for reinsurance purposes and control over the conclusion of reinsurance contracts with other insurance organizations on the national market. It should be noted that three insurance companies are currently in the process of liquidation, and the insurance license has been suspended for three companies as well [*The main performance indicators of insurance organizations...*].

By the end of 2017, Belarusian state insurance companies did not provide the growth parameters stipulated in the Republican program for insurance market development for 2016–2020, which are: to ensure the growth rate of insurance premiums for all types of insurance at 184 percent by the end of 2020 in comparison with 2015; to increase the volume of insurance premiums per capita 1.8 times; to achieve a ratio of insurance premiums to gross domestic product at the level of 1.05 percent by 2020 (with a projected 166.5 percent growth rate of gross domestic product in current prices in 2016–2020); the ratio of assets of insurance organizations to the gross domestic product should reach at least 3.1% [*The state program for the development...*].

However, as an analysis of the insurance sector of the Republic of Belarus in 2015–2017 shows, its development was more dynamic. Thus, insurance companies managed to increase the ratio of their assets to the gross domestic product from 2 percent (as of January 1, 2011) to 2.7 percent (as of January 1, 2018). During the year 2017, insurance companies’ contribution in direct insurance and co-insurance reached the level of 1,050.8 million rubles. The growth rate of insurance premiums for 2017 compared to the same period in 2016 amounted to 106.4%. For voluntary types of insurance for 2017, insurance premiums amounted to 605.6 million rubles, which is 63.5 million rubles more than in the same period in 2016. The insurance premiums for the compulsory types of insurance in 2017 reached the level of 445.2 million rubles, which is 0.6 million rubles less than in 2016. The share of voluntary types of insurance in the total amount of insurance premiums is 57.6% (in 2016 this indicator reached the level of 54.9%). Insurance compensation payments and insurance coverage in the whole country amounted to 532.3 million rubles, which

is 8.5 million rubles less than in the same period in 2016. The level of insurance payments in the total amount of insurance premiums in 2017 was 50.7% (for 2016 reached the level of 54.7%) [*The main performance indicators of insurance organizations...*].

The main efforts in the insurance market are devoted to the development of voluntary insurance. These measures are represented by the introduction of new insurance products and expansion of the practice of applying common voluntary insurance conditions to simplify the understanding and choice of specific insurance services by insurers. Other measures include increasing the availability of insurance services through the development of remote interaction forms with customers, and creation of a competitive environment with the elimination of preferences in the activities of insurance companies.

Attention should be paid to the development of the co-insurance mechanism and reinsurance since the transfer of risks abroad means a significant outflow of foreign currency funds from the country. Taking into account the low capitalization of the insurance market in the Republic of Belarus in comparison with foreign markets, the reinsurance system is very important for its development and stability.

By 2020, the insurance market of the Republic of Belarus should have a degree of financial stability and competitiveness, which allows resisting the challenges associated with the influx of financial services to global players with greater opportunities on the domestic market.

3. Formation of the financial stability mechanism of insurers in the framework of creating insurance pools

The process of implementing the new requirements in the EU for insurers' solvency (Solvency II) provides a review of priorities in the supervision and monitoring of the activities of professional participants in the insurance and reinsurance markets – from supervision aimed at compliance monitoring with the insurance legislation, to risk assessment. In this regard, the task of developing and implementing internal monitoring systems for insurers' activities on the basis of risk assessment methods becomes urgent for their financial stability and reliability.

There is no comprehensive research of these problems in insurance, in spite of the fact that there are specific features in this field of activity. To some extent, the issues of the financial status of insurance organizations have been covered in the works of A. Arkhipova, I. Balabanova, T. Verezubova, M. Zaitseva, M. Karpitskaya, G. Nasyrova, L. Orlanyuk-Malitskaya and others.

At the moment it is necessary to adapt the European insurance legislation and its transformation, taking into account specific problems of insurance development in the Republic of Belarus.

The financial stability mechanism of insurers provides the necessity to form a financial stability management system and identify the subjects of this system. The main elements of the mechanism are the system of legal, organizational, economic and financial provisions of financial stability of insurers and reinsurers. At the macro level the following methods of managing financial stability can be identified: licensing, regulation, supervision, rating, audit; whereas at the micro level these methods are: diversification, retrocession, internal audit, investment.

The economic result of the effectiveness of the financial stability management on the insurance market should be stabilization of the insurance market in general and an increase in the share of the insurance market in GDP.

A reinsurance pool can serve as an application tool for managing the financial stability of individual insurers and stabilizing the insurance market as a whole.

The reinsurance pool, in our opinion, should perform the following main functions:

- to develop and implement, on behalf of all participants, the administration of insurance contracts (insurance policies), including statistical market research and actuarial calculations necessary for the calculation of unified tariffs;
- to carry out, on behalf of the participants, the settlement of losses, including the acceptance of applications for reimbursement, loss assessment procedures, the calculation and direct payment of compensation;
- to reinsure their risks both on the national and international reinsurance market [Karpitskaya, 2016, p. 74].

From our point of view, the reinsurance pool can be described as a system in which insurers, under a voluntary agreement or in accordance with the legislation, transfer all reinsurance risks to the reinsurance pool [Karpitskaya, 2017, p. 3925].

Therefore, it is advisable to strengthen the state role in creating reinsurance pools for the most significant and unsafe operations: specific energy, road, agricultural, and natural disaster risks. This will help to create the conditions for the further development of reinsurance pools of significant risks and risks.

In our opinion, the participants should include highly reputable insurance and reinsurance companies, including foreign ones, as well as the state. The most important participant in the reinsurance pool is the general reinsurer, who performs the manager's duties. Often, he is also the founder of the pool. In addition to the earned percentage of profits as a member of the pool, the general reinsurer is rewarded for the guidance. The functions of the general reinsurer are as follows: cash flow management; the regulation of guarantee obligations by all participants; establishment of liability limits, types of accepted risks, their concentration; retrocession coverage acquisition; the establishment of minimum requirements for assignors and participants; ongoing monitoring of

the pool; provision of all management procedures; the establishment of payment mechanisms for all types of commissions and bonuses. These measures provide a solution to key problems and disagreements and the implementation of risk management [Krupenka, 2015, p. 140].

It is necessary to provide the participants of the reinsurance pool with the right to independently determine their own retention when reinsuring risks, within the framework of state support, which means the abolition of the 20% minimum liability standard of the reinsurer's own capital.

4. Priorities in the insurance development strategy in the Republic of Belarus

According to recent experience, in market conditions those insurance companies that develop strategic steps to determine the optimal ways of forming an effective mechanism for managing insurance activities, taking into account international experience, are the most stable. At present, the development of a long-term Strategy for the insurance sector at the international level has attracted the close attention of the insurance community. There is no doubt that in the process of developing a Strategy, the responsible government bodies in each country take into account the opinions and proposals of insurers, the state, and other stakeholders.

The formation of a new development strategy for the Belarusian insurance market should include practically manageable tasks at this stage of its development and simultaneously take into account international trends. In our opinion, the Strategy should be based on the following principles:

- 1) socio-economic goals in accordance with the main public policy initiatives;
- 2) compliance with the requirements of the WTO, the Eurasian Economic Space, and other key international standards and regulations;
- 3) use the experience of foreign insurance market development;
- 4) stability, transparency, and globalization of the insurance business.

In our opinion, the development of the strategy should include the following stages:

- 1) developing a vision and strategy for both the market in general and for the main components of the market;
- 2) introduction of the operational plan;
- 3) development of tasks for the participants with a definition of specific coordination functions for each participant.

This approach in developing a national strategy will ensure harmonization with international practice.

In the future, taking into account the implementation of measures to change the ownership structure in the economy of the Republic of Belarus, the strength of economic integration, and creation of a common financial market within the framework of the EAEU, in the implementation of a national rating system it

will be necessary to assess the insurer's rating position and detect its influence on the reliability of the insurance market as a whole. In order to assess the reliability of the insurance market, it is necessary to determine the standard deviation reliability (formula 1):

$$\delta = \sqrt{\sum_{i=1}^n (k_i - R_i)^2 \times W_i} \quad \text{formula (1)}$$

where

- δ – standard deviation reliability;
- n – the number of groups of indicators according to the methods of financial stability and reliability of the insurer;
- i – the number of groups of indicators according to the methods of financial stability and reliability for a specific insurance organization;
- k_i – the average value by groups of indicators according to the methods of financial stability and reliability of the insurer in general for the market;
- R_i – the average value by groups of indicators according to the methods of financial stability and reliability of the insurer for a specific insurance organization;
- W_i – the specific weight of the importance of the group of indicators according to the methods of financial stability and reliability of the insurer.

The financial stability coefficient of insurers influence on the stabilization of the insurance market allows us to assess the level of influence when the coefficients in the groups of indicators according to the methods of financial stability and reliability of insurers differ from each other (formula 2):

$$K_c = \frac{\delta}{DR} \quad \text{formula (2)}$$

where

- K_c – the coefficient of insurers' financial stability influence on stabilization of the insurance services market;
- δ – standard deviation reliability;
- DR – the sum of the average values by groups of indicators according to the methods of financial stability and reliability of the insurers in general.

When comparing insurers in terms of their financial stability, the greatest impact on the stability of the insurance market is the one which has the highest K_c value.

Thus, the advantage of this approach is the ability to predict the future development of the insurance market on the basis of a small sample, taking into account a number of possible scenarios. The practical significance is represented by the potential of using it to formulate and refine long-term policy documents related to the insurance market development in the Republic of Belarus, taking into account the ongoing integration processes.

It is necessary to propose the development and implementation of standardized conditions for certain types of retail insurance, representing the minimum insurance protection level and quality standards (real estate appraisal, compensation procedures, insurance payment).

5. Conclusions

As a result of the research, a theoretical substantiation of the fundamentals of the financial system functioning was made. The role of all subjects within this system in the effective development of the country's economy was shown. The factors at the macro and micro levels which negatively affect the development of the financial system are identified. The insurance market is given a special role in the research. The influence of factors on the level of insurance coverage demand is given. The proposals for improvement of insurance in the Republic of Belarus through the development of the insurance and reinsurance system within the entire financial sector of the Republic of Belarus are made in the article. The proposals take into account the trends in state regulation of insurance activities, and suggest tools for ensuring the financial stability of reinsurers. Approaches to the development of insurance protection have been rendered by the introduction of additional compulsory insurance types. The authors propose establishment of a communication mechanism within the insurance market as a basis for the Strategy for the development of the Belarusian insurance market.

An effective insurance activity mechanism was developed within the functioning framework of the financial system. The role of insurance organizations as a stabilizing factor in the financial market, and the necessity of insurance and reinsurance pools, is justified. These measures allow diversifying risks, reducing their accumulation, and ensuring reliable development of the insurance market.

Approaches to the insurance market development strategy are offered in the article, which will allow taking into account not only the specific functioning of insurance and reinsurance companies, but also the ongoing integration processes in the insurance market.

The developed set of measures to stimulate a demand for insurance will allow to develop the necessary incentives for insurance for enterprises and households.

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Thus, with the effective and reliable development of the insurance market, the entire financial system can be fully developed, ensuring stable economic growth at the same time.

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