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World financial crisis:
causes, consequences, ways of overcoming

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World financial crisis: causes, consequences, ways of overcoming

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Goal of the monograph's publication: generalization of ideas of prominent researchers from different countries of the world regarding the causes and consequences of the world financial crisis, determination of specific features of its development in different countries, generalization of experience regarding the ways of overcoming the crisis.

General outline:

- Author's vision of the causes of the world financial crisis.
- Peculiarities and general features of the financial crisis in the country represented by the author.
- Methods used by the government of the author's country to fight the crisis and the author's comments regarding their efficiency.
- Author's vision of ways to overcome the world financial crisis.
- Author's vision of global consequences from the world financial crisis.
- General conclusions.
- References.

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Development trends of the Ukrainian insurance market since its creation and during the financial crisis

Abstract

The article provides a retrospective analysis of the development of Ukraine's insurance market since the creation of Ukraine as an independent state. The emphasis is put on the main positive characteristics of this market, the unused opportunities and future potential. It gives the data on some insurance companies for the past years with special attention to the insurance market dynamics at the end of 2008 and at the beginning of 2009, i.e. during the world financial crisis. The special features defining the crisis situation on the insurance market of Ukraine are given.

Keywords: insurance market, financial crisis, indicators of insurer's activities, insurance market regulation.

1. Problem statement

During the process of its formation and development, the insurance market of Ukraine has faced a great number of serious problems, which are studied by the national researchers and practitioners. According to the most experts, the Ukrainian insurance market encountered serious problems even before the financial crisis. These difficulties were the direct consequences of lack of system for the regulation of the state economy, legislation deficiencies, and underdevelopment of the financial market in general. It is believed that the financial market in Ukraine is still not performing the functions it is supposed to perform, in particular, the mobilization of capital for the development of the economy's real sector and efficient resources allocation.

The purpose of the articte is to study the main problems of the Ukrainian insurance market in recent years, especially in the conditions of the world financial crisis, and the influence a state regulation has on it.

2. The main part

During the first years of the Ukrainian insurance market formation there was a fast growth of the number of insurance companies: in 1991 there were only 28 insurance companies in Ukraine, in 1992 – 171, in 1993 – 455, in 1994 – 616, and in 1995 – 655. However, everyone understands that a huge number of the newly created companies does not necessarily mean the creation of a fully fledged insurance market.

The particular feature of profits amassing by most of these companies was the activity based on the principle of "financial pyramids" or speculation based on hyperinflation processes. Small statute funds of insurers and low insurance reserves led many insurance firms to bankruptcies.

It should also be said that in the developed countries the licensing and regulations pertaining to the statute capital are the main barriers to enter the insurance market. During the initial stage of the insurance market formation in Ukraine we had low cost of licenses and poor requirements of regulatory authorities to insurers. In other words, licensing played a secondary role in the formation of entry barriers. Ownership capital also did not play a deterrent role.

However, in spite of these problems, the insurance market of Ukraine received a real impulse for further development. The insurance of property became the priority area for the national insurers.

The main legislative act (the Law of Ukraine), which regulated the functioning of the insurance market, was enacted in 1996. This was the law of Ukraine "On insurance". Also, the new regulations were adopted for the formation of the statutory fund of an insurance organization concerning its liquidity, solvency and reserves. The insurers were obliged to develop insurance rules for all types of insurance and to have them approved by the supervisory authority. The enactment of this law led to changes in the structure of the insurance market and insuring companies, as well as the process of their formation and development.

In 1997, the procedure of re-registration of insurers was introduced. As a result, the licenses of 325 insurance companies were nullified. Almost immediately the number of insurers began to grow again, but on different conditions.

At the end of 2001, there were some changes in the Law of Ukraine "On insurance". From that moment, the authorized fund of an insurer had to be no less than 1 million Euros for companies working with the risk types of insurance, and 1,5 million Euros for insurers carrying out life insurance.

Given the importance of strengthening the state regulation and effective supervision over the activities of insurers, the State Commission on the regulation of financial services market was founded in 2002. In the first years of its existence the Commission did not have a sufficient number of qualified experts and possessed limited technological abilities, which hampered the analysis of the insurers' activity and evaluation of their risk levels.

A special feature of the insurance market development at that time was the growth of "financial insurance", i.e. the insurance, which is carried out by organizations in order to optimize their profits. In 2003, the share of this type of insurance in the general structure of insurance premiums amounted to 75 per cent, or 6.8 billion Hryvnias.

Pseudo insurance, i.e. the use of insurance for funneling the resources into the shadow economy was a high barrier on the way towards the efficient development of insurance market. According to different evaluations, the share of such insurances could be from 30 up to 60 per cent of the country's insurance market. It should also be pointed out that the insurance market is often used to reduce the volumes of tax payments in other branches of the economy by means of insuring and reinsuring financial risks by buying short-term policies for reducing the taxation base.

In 2005, the Supreme Council of Ukraine adopted the Conception for the development of Ukraine's insurance market for the 2005-2010 period, which set the priorities of the insurance market and offered mechanisms for the market coordination.

The Development strategy of Ukraine's financial market till 2015 has the following mission: to create an efficient financial sector in Ukraine capable of providing the necessary resources and services to the real sector of the economy, to contribute to the country's social development, its integration into the world financial structures and avoid threats to the national interests and economic security of the country.

The priority areas of the development are defined as follows:

- improvement of competitiveness and stability of financial institutions;
- increase in the volume and quality of financial services;
- protection of interests of financial services' consumers;
- enlargement of the range of financial services;
- implementation of reforms of state regulation in order to raise its efficiency;
- international integration of Ukraine's financial market.

The interest of foreign financial groups in the Ukrainian insurance market has been on the rise since then. With the growing number of companies with foreign capital the market is becoming more civilized, however, this segment still remains insignificant in the financial market of Ukraine (see Table 1).

The Conception pointed out that apart from positive microeconomic indicators there were also preconditions for the development of the national insurance market: increase in the population income, growth of interest in property protection, growth in the number of dynamically developing companies, introduction of compulsory insurance for car owners, development of the market of financial services and mortgage loans, introduction of non-state pensions schemes.

Table 1. Dynamics of the financial sector of Ukraine 2007-2008

Segment of the financial sector of the economy	Indicators				Growth rates, per cent
	Total amount, bln. Hryvnias	Share in total assets, per cent	Total amount, bln. Hryvnias	Share in total assets, per cent	
	2007		2008		
Banking sector	599,4	93,6	926,1	94,7	54,5
Insurance companies	32,2	5,0	41,9	4,3	30,2
Credit unions	5,3	0,8	6,1	0,6	14,4
Financial companies	3,3	0,5	3,0	0,3	-10,0
Non-state pension funds	0,3	0,04	0,6	0,1	117,8
Total	640,5	100,0	977,7	100,0	52,6

At the same time, there were factors that hampered the development of the insurance market, in particular: imperfection of the system for the protection of insurance services consumers; low level of re-insuring by domestic companies; small customer base of insurers; concentration of activities mainly on the property insurance of legal persons; underdevelopment of long-term life insurance; lack of legal regulation of insurers' activity in the area of compulsory medical insurance; a great number of companies with low level of capitalization; insufficient professional training of insurance companies' personnel; low level of the population's insurance culture.

The dynamics of insurance companies' number is presented in Table 2. As we see, the development of the global financial crisis did not have an impact on the tendency towards the growth of the insurance companies on the Ukrainian market.

Table 2. Number of insurance companies in Ukraine

Indicator	Number of insurance companies by the end of the year							
	2002	2003	2004	2005	2006	2007	2008	First quarter 2009
Number of insurance companies	338	357	387	398	411	447	469	477
- life insurance		30	45	50	55	65	72	75
- others		327	342	348	356	382	397	402

Therefore, the insurance market has a large potential, although the growth trends remain insignificant (Table 3), and considering the financial crisis, some areas have been experiencing stagnation in their development (Table 4).

Table 3. Indicators of insurance companies activities in Ukraine

Years	Indicators					
	Insurance premiums, mln. Hryvnias	Insurance premiums per insurer, on average, thousand Hryvnias	Insurance payments, mln. Hryvnias	Insurance payments per insurer, on average, thousand Hryvnias	Level of insurance payments, per cent	Number of insurers
1998	789,16	3 107	177,85	700	22,5	254
1999	1164,15	4 426	360,92	1 372	31,0	263
2000	2136,00	7 547	407,00	1 438	19,1	283
2001	3030,51	9 239	424,21	1 293	14,0	328
2002	4442,13	13 142	543,10	1 607	12,2	338
2003	9135,30	25 639	860,60	2 410	9,4	357
2004	19431,40	50210	1540,30	3980	7,9	387
2005	12853,50	32295	1894,20	4759	14,7	398
2006	13829,90	33649	2599,60	6325	18,8	411
2007	18008,20	40286	4213,00	9425	23,4	447
2008	24008,60	51191	7050,70	15031	29,4	469
First quarter 2009	4677,2	9805	1507,20	3159	32,2	477

Table 4. Dynamics of the main indicators of insurance market, 2007-2009

Indicators	First half-year 2007	Second half-year 2007	First half-year 2008	Second half-year 2008	First half-year 2009	First quarter. 2008/First quarter 2009	
						Mln. Gryvnas.	Per cent
Number of insurance contracts signed in this period							
Number of contracts apart from agreements of compulsory traffic accidents insurance, which include:	8885441	11 294 499	11 246 303	11 582 428	9 549 050	-1 697 253	-15
- contracts with insured physical persons	7 186 125	9 261 214	8 869 284	9 816 186	8 142 250	-727 034	-8
Number of agreements of compulsory personal insurance against transport accidents	281 996 295	297 590757	322 660 450	330 508 377	267 822 226	-54 838 224	-17

Table 4 (cont.). Dynamics of the main indicators of insurance market, 2007-2009

Indicators	First half-year 2007	Second half-year 2007	First half-year 2008	Second half-year 2008	First half-year 2009	First quarter. 2008/First quarter 2009	
						Mln. Gryvnas.	Per cent
Insurance activity, mln. Hryvnias							
Gross insurance premiums	7 673,1	10 335,1	11 279,5	12 729,1	9 514,0	-1 765,5	-16
Net insurance premiums	5 325,6	7 028,2	7 601,9	8 379,9	6 313,4	-1 288,5	-17
Gross insurance payments	1 784,7	2 428,3	3 376,0	3 674,7	3 275,5	-100,5	-3
Level of gross payments, per cent.	23,3	23,5	29,9	28,8	34,4	4,5	15
Net insurance payments	1 599,9	2 284,1	3 223,5	3 322,6	2 916,7	-306,8	-10
Level of insurance payments, per cent.	30,0	32,5	42,4	39,6	46,2	3,8	9
Re-insurance, mln. Hryvnias							
Paid for re-insurance, including:	2 772,2	3 651,7	4 229,4	4 835,2	3 754,3	-475,1	-11
- to re-insurers – residents	2 347,5	3 306,9	3 677,6	4 349,2	3 200,5	-477,1	-13
- to re-insurers – non-residents	424,8	344,7	551,8	486,0	553,8	2	0
Payments of compensations to re-insurers including:	239,2	415,5	418,5	508,0	471,5	53	13
- to re-insurers – residents	184,8	140,9	152,3	352,4	358,9	206,6	136
- to re-insurers – non-residents	54,4	274,6	266,2	155,7	112,6	-153,6	-58
Received insurance premiums from re-insurers–non-residents	51,6	60,6	115,4	202,1	131,6	16	14
Payments compensated to re-insurers-residents	113,0	391,1	436,1	619,5	392,9	-43,2	-10
Insurance reserves, mln. Hryvnias							
Volume of insurance reserves	6 256,8	8 423,3	9 127,2	10 904,1	9 619,6	492,4	5
- reserves from life insurance	762,2	991,3	1 166,5	1 609,0	1 603,6	437,1	38
- technical reserves	5 494,6	7 432,0	7 959,9	9 295,1	8 016	56,1	0,7

Table 4 (cont.). Dynamics of the main indicators of insurance market, 2007-2009

Indicators	First half-year 2007	Second half-year 2007	First half-year 2008	Second half-year 2008	First half-year 2009	First quarter. 2008/First quarter 2009	
						Mln. Gryvnas.	Per cent
Insurers' assets and authorized capital, mln. Hryvnias							
General assets of insurers	26 274,30	32 213	35 561,7	41 930,5	41 999,5	6 437,8	18
Assets defined by Article 31 of the Law of Ukraine "On insurance" for providing resources of insurance reserves	16 410,90	19 330,3	20 852,2	23 904,9	22 947,2	2 094,9	10
Volume of paid authorized funds	9 351,70	10 633,6	11 970,5	13 206,4	13 627,1	1 656,6	14

Let us now move on to a more detailed characteristic of the dynamics of the Ukrainian insurance market in the last years.

Today, we have the following positive results in the development of the domestic insurance market:

- real growth of all kinds of insurance operations;
- growth of insurance payments;
- structural changes in favor of a voluntary insurance and its long-term types;
- increase in the number of insurance contracts signed with the help of insurance brokers;
- increase of indicators of insurers' financial reliability, formation of financial groups with the participation of insurers.

Gradually, the domestic insurance market is experiencing an increase in number of insurance companies with foreign capital. By the end of 2007 their number rose to 78, 8. The major investors are the United Kingdom – 34 per cent, United States – 17 per cent, Denmark – 10 per cent, Poland – 9 per cent, Austria – 6 per cent, and others.

According to the results of 2008, one can also speak about the considerable problems in the insurance area:

- 3 companies became insolvent (their payment reserves were smaller than necessary);
- the total reserve fund formed by 441 insurance companies amounted to 13,2 bln. Hryvnias. For 43 of these companies it was less than 5 thousand Hryvnias;

- free reserves, which had to be made by insurance companies in order to insure the financial solvency, were formed only by 81 insurers (in total amount of 2,8 bln. Hryvnias).

The analysis of scientific literature, first of all the publications of V. Furman, L. Harin, D. Navrotsky, A. Vasylenko and V. Trynchuk, makes it possible to summarize the main problems (weaknesses) facing the insurance market of Ukraine. These problems are as follows:

- *economic* (low demand for insurance services, imperfect capital structure of insurers, underdevelopment of investment instruments for long-term distribution of insurance reserves);
- *legal and organizational* (underdeveloped traditions in the investment environment of the insurance market; increasing number of insurers, which is not matching the growth in demand; lack of adequate state policy in the field of insurance; lack of regulatory acts, which should regulate the insurance market activity; a great deal of legally defined types of compulsory insurance and problems with their financial backup; relatively weak life insurance sector; poor regulation of the insurance intermediaries activity; poor regulation in the field of obligatory medical insurance; the creation of insurance market in parallel with the development of legal provisions, not always adequate;
- *functional* (underdevelopment of the market of insurance intermediaries, discrepancy between the level of insurance development and high market demands; low profitability of certain types of insurance; low professional level of employees, lack of insurance technologies);
- *informational and analytical* (non-transparency of the insurance market; lack of statistical data about the state of the insurance market; imperfection of insurers' financial reporting; lack of efficient ratings of insurance companies; non-transparency of data about the ownership structure of the domestic insurance market);
- *socio-psychological* (ignoring the interests of insurers for a prolonged time, lack of trust to insurance companies; emergence of certain branches of the economy (agriculture, transport, foreign tourism, where the level of trust deficiency to insurers is critical).

At the same time, we can indicate the following strengths (advantages) of the insurance market:

- *economic* (dynamic growth of operations on the insurance market; steady growth of collected insurance premiums; development of the insurance market with the gradual increase of insurance companies' capitalization; growing activity of foreign investors);
- *institutional* (growth of insurance companies, their involvement in insuring banking and financial capital; formation of the system of mortgage crediting; capital concentration

and creation of insurers' amalgamations on the basis of their commercial and financial interests; strong positions of insurers' amalgamations);
- *socio-psychological* (international recognition of the insurance market; raising the interest of legal and physical persons in the defense of their property);
- *regulatory* (the existence of tax preferences on life insurance; more emphasis on the regulation of insurers' financial stability; liberalization of insurance supervision; rise in mergers and acquisitions, change of owners and top managers of some of the insurance companies, the emergence of a more aggressive policy).

The world financial crisis has deprived the Ukrainian financial market of some of its advantages and potential opportunities. For example, the economic situation in the country has significantly deteriorated, what is evident from the decline in the GDP growth, increasing inflation, destabilization of the state currency, declining income of the population, reduction of efficiently functioning enterprises. The influence of the world financial crisis on the economy of Ukraine can be demonstrated by the following:

- the trade balance in 2008 was 18,5 bln. dollars (compared to 11,3 bln. in 2007);
- the gross foreign debt reached 103,2 bln. dollars, of which 39,4 bln. dollars were the debts of banks;
- the exchange rate Hryvnia/Dollar fell by 52,5 per cent.

Concerning Hryvnia devaluation, this process had a serious impact on the insurance market, especially the growth of insurers' losses, decrease in the number of insurance contracts in "classis insurance", rapid decline in the paying capacity of insurers.

According to the results of the first quarter of 2009, there was an obvious decline regarding the majority of insurance indicators in comparison with the first quarter of 2008. The dynamics of the indicators is indicative of the following trends:

- the number of contracts fell by 15 per cent, while the number of contracts signed with physical persons decreased by 8 per cent (with the exception of contracts of compulsory traffic accidents insurance);
- the volumes of gross insurance premiums fell by 16 per cent, while the volume of net insurance premiums fell by 17 per cent;
- insurance payments decreased by 10 per cent: gross insurance payments fell by 3 per cent, net insurance payments fell by 10 per cent;
- the volume of re-insurance fell by 11 per cent, including the volumes of premiums paid on the internal market – by 7,1 per cent, and by 17,8 per cent – on the external market;

- the volume of insurance reserves fell by 5 per cent;
- total assets increased by 18 per cent, including the assets defined by the legislation for the provision of insurance reserves – by 10 per cent;
- the number of insurance companies has increased by 4,1 per cent (19 companies). By the end of the first quarter of 2009, the overall number of insurance companies was 477, including 75 life insurers (an increase by 6 companies) and 402 non-life insurers (an increase by 13 companies).

According to the experts of the State commission for the regulation of financial markets, the insurance market has confronted the problem of deepening of the whole range of risks caused by:

- fall of the stock market;
- increase of risks connected with the investment of assets of financial organizations, defaults on loans;
- distrust of the population to financial institutions because of the refusal of the latter to fulfill their contract obligations;
- currency instability;
- lack of coordination between banks and non-banking financial institutions;
- negative inflationary expectations of the populations;
- growth of the "shadow" economy;
- re-evaluation of investment assets through currency, credit and other risks, which can lead to the reductions of volumes of financial institutions' net assets

The insurance companies are facing a lot of serious problems during the financial crisis:

- refusal of banks to return depositors' money (as of 17,07.2009 banks had 144 mln. Hryvnias of frozen assets belonging to insurance companies);
- inability of the insured physical persons to fulfill their obligations – payments for insurance contracts in foreign currencies;
- providing the reliable saving of insurance reserves in the banking system.

During the development of the world financial crisis the State commission for the regulation of financial markets set the following objectives: development of anti-crisis plan, improvement of cooperation with the National Bank of Ukraine, implementation of steps aimed at elimination of irresponsible insurance companies from the market.

The Commission also defined the steps that should be undertaken within anti-crisis activities:

- access of insurance companies to the reserves placed at banks' deposits on the basis of the decision of the National Bank of Ukraine;
- consultations with the National Bank of Ukraine and making decisions regarding the possible recapitalization of non-banking financial institutions;
- improvement of functional mechanisms for temporary bank administrations;
- lifting of harsh restriction concerning the level of credit ratings for investments into the assets of insurance companies;
- creation of opportunities for the compensation of losses of the population as a result of non-banking financial institutions insolvency;
- together with the National Bank of Ukraine, to create a Fund of guaranteed insurance payments by using the insurance reserves of insurance companies on the accounts of the National Bank of Ukraine and organization of currency auctions;
- preparation of strategic documents, which would regulate the development of the financial and insurance market (Development strategy of the financial sector of Ukraine till 2015; Conception of protection of rights of financial services' consumers).

The Commission has also developed a plan of its activities, which include:

- transition of the Commission to the prudential supervision based on risks;
- introduction of the system of control over the irresponsible advertisement of insurers in order to avoid phenomena such as dumping;
- introduction of changes into the Law of Ukraine "On insurance";
- development of the legal regulation for the insurance of agricultural risks;
- creation of mechanisms for the introduction of insurance medicine.

Conclusions

It is necessary to point out that in spite of the considerable decline in all the parameters of the Ukrainian insurance market, this segment of the financial market still remains promising for further development (on average, a citizen of Ukraine spends less than a dollar on insurance), especially in the area of life insurance, pension and medical insurance. Considering all of this, it is possible to make a conclusion about the growth and development of this market in the near future.

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