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New regulations in the development of a financial market

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Effective functioning of a financial market has a key role in the development of a country's economy. Developing countries experience lack of funds, one of the best ways to attract investment capital is the development of the right direction of the securities market, credit market and insurance market that are served by the regulations adopted in this field, which are derived from the Association Agreement.

It can be said that a new phase starts with new regulations on the market of financial institutions. Current regulations are directed to the solvency of the insurance company, the use of mechanisms for maintaining financial sustainability, and the rule of formation and placement of reserves. However, there are no regulations for the development of life insurance. According to the new regulations, we think that in 2019 banking sector will be significantly different from the 2017 situation. In the short term, it will bring down retail lending, increase expenditures in the sector, increase demand on capital and reduce profitability, and in the long term we should hope that it will contribute to the improvement of the financial system of Georgian financial system, which will ensure financial sustainability of the banking system. Regulations concerning the development of the securities market, here a pension reform is important, which has come into force since January, 2019. As a result of this, the state accumulative pension system started in which large amounts of accumulated funds will be invested in local securities, in the local economy.

The research objective: To determine the effectiveness of new regulations on the financial market, the purpose of implementing regulations is to improve the quality of the banking system, the securities market, the insurance market, and the sustainable development of the economy.

Key words: Insurance Market; Securities Market; Banking Market.

Introduction

Effective functioning of a financial market has a key role in the development of a country's economy. Developing countries experience lack of funds, one of the best ways to attract investment capital is the development of the right direction of the securities market, credit market and insurance market that are served by the regulations adopted in this field, which are derived from the Association Agreement.

Insurance Financial Market

One of the oldest history of financial institutions is the development of insurance industry. The initial signs, which were meant to compensate losses during unfavorable events, first appeared in ancient Rome BC. The primary requirement for establishing insurance relations was the formation of a relevant fund for covering insurer's liabilities with insurance contributions. However, the purpose of the insurance funds before transferring to commercial principles was only a compensation.

Alongside with the main purpose, transfer of commercial funds to the commercial principle, gave them the investment

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direction. The financial market developed for investing was a necessary condition. Unlike financial institutions, insurance institutions are characterized by peculiarities, since its activity depends on the realization of the risks associated with reimbursement. Therefore, the investment direction of the insurance reserves is also different from the investing objectives of other types of companies. Regulatory laws and normative acts of the insurance sector are designed to maintain and sustain insurance funds.

The emergence of the first product in the history of insurance is related to marine risk insurance in the XIV

century. However, the signs of investing in the fund created for reimbursement of the damage caused by this type of risk did not appear until the commercialization of the insurance case. In the XVII century, the development of mathematical statistics and its dependent actuarial deposits made it possible to create a life-long long-term insurance product.

Long-term and accumulated pension insurance in the advanced countries of the world in the modern period holds leading position in the provision of a financial market with financial resources, which is proved by the data below

Table №1: The share of life insurance premiums paid on the insurance market

Year	2010	2011	2012	2013	2014	2015	2016	2017
	▲▼	▲▼	▲▼	▲▼	▲▼	▲▼	▲▼	▲▼
Country								
Australia	57.0	56.7	53.6	54.9	61.1	59.2	55.4	52.1
Austria	..	..	..	34.1	35.5	35.3	32.5	31.7
Belgium	65.0	63.2	64.7	57.7	56.5	55.4	54.4	53.7
Canada	35.6	34.0	32.1	32.9	28.7	28.7	..	..
Chile	66.0	62.5	65.5	66.5	65.8	68.3	70.4	69.4
Czech Republic	46.0	46.4	46.9	45.7	45.1	41.1	40.6	38.3
Denmark	..	68.2	68.7	95.4	67.7	68.9	68.7	69.1
Estonia	40.6	39.8	33.9	29.3	30.3	31.2	30.0	27.3
Finland	59.5	51.2	51.2	56.8	57.4	58.3	50.6	50.7
France	17.2	63.9	62.1	62.4	64.2	64.2	58.0	55.2
Germany	47.9	45.7	35.5	36.0	35.9	34.0	33.1	32.1
Greece	43.3	43.7	43.2	41.4	49.5	50.5	47.2	50.4
Hungary	53.2	54.6	53.0	54.5	54.8	51.1	49.5	48.2
OECD - Total								

Source: Organization for Economic co- Operation and development, <https://stats.oecd.org/Index.aspx?DataSetCode=INSIND>, insurance indicators

As the table shows, the annual life insurance share is increasing on the insurance market, thus the possibility of investing in insurance companies is increasing, which also increases a financial market resource potential. The history

of the insurance industry in Georgia is about 28 years old. The share of investment in total revenues shows the state of investment function.

Table №2: Financial data of Georgia's insurance market (2010-2018)

Insurance Market	Total revenues	Investment Income, Gel, Life Insurance Fund Investment	Life insurance coverage on the insurance market
2010	38 854 326	9 341 248	2,77%
2011	(20 353 044)	6 706 533	5,10%
2012	(5 893 620)	6 944 339	4,39%
2013	3 205 870	5 746 170	2,67%
2014	44 703 072	4 806 083	5,50%
2015	4 757 925	5 461 982	6,95%
2016	25 903 033	6 743 317	6,46%
2017	26 053 415	8 055 176	5,60%

Source: State Service Supervision Service of Georgia: <http://insurance.gov.ge/Home.aspx>

According to the data provided in the table, the share of life insurance in Georgia is very low, and the investment activity of companies is also low. The experience of European countries in the development of life insurance

markets is very interesting. The history confirms that the establishment of a life insurance market in European countries began with the Roman Agreement in 1957 and is now is a strong industry in each country. In 1992, the life

insurance market was established with the integration to the European Union. The development of the market, along with the legal regulation, should also be assisted by the numerous increase of insurance policies, and for this purpose, the National Government encouraged its population to purchase the insurance policy by the conceded taxation regime, which increased the company's mathematical reserves and created investment opportunities.

Insurance activities in Georgia are carried out by the State Insurance Supervision Service, which is the law successor of the National Bank in cases of Insurance and Pension Schemes Supervision, including the status, rights and obligations related to the membership of the International Association. Current regulations are directed to the solvency of the insurance company, the use of mechanisms for maintaining financial sustainability, and the rule of formation and placement of reserves. However, there are no provisions for the development of life insurance. Introduction of solvency directives in Georgia is important for integration with the European Union. In the EU countries until January 1, 2016, the Solvency I directive was in action, after which they activated the Solvency II directive, which ensured the financial sustainability of insurance companies. In the Georgian legislation this directive shall be reflected in 2020. Its main demand is that insurance companies must have enough financial resources and solid guarantees. It also establishes management and supervision rules. According to this directive, insurance companies are required to have two types of capital:

- Minimum Capital Requirement (Minimum Capital Requirement): The minimum amount of capital, under which the policy holders will be unprotected from the high risk.

Increasing financial sustainability will increase the trust of the population to insurance companies, only after that, it will be possible to share EU experience for life insurance expansion.

The Association Agreement between the EU and Georgia during the period 2017-2020 focuses on providing life insurance services between the parties in the format of communication. This Agreement will bring the long-term insurance conditions in line with EU standards in the agenda.

The important issue of economic development and market principles of Georgia is to ensure the financial sustainability of the banking system, the Georgian banking sector is dynamically developing, it is healthy and is making important contribution in the development of the Georgian economy.

During the last two years, the National Bank of Georgia has developed, improved and implemented important new regulations.

In order to establish a new bank regulation structure in Georgia, it should first of all define the legislative basis. The proposed amendments can be divided into two blocks, first of which concerns the sustainability of capital banks and the problem of impairment was named as the main motivation for the second regulation.

After the NBG had united online loan companies under its regulations, it introduced the prudential norms for microfinance organizations, it became a signal for the segment's rapid consolidation, the rise of capitalization and

the leave of unqualified players from the market, the process we are watching now. The NBG also makes a statement on the introduction of the definition for "loan issuer" body and all the bodies subject to it shall comply with the regulation. One of the main tasks of the government in this process is to create an equitable and fair ecosystem for all, big and small players of the market.

According to the regulations already implemented, it can be said that the number of microfinance organizations registered in the National Bank of Georgia reduced by 5, the number of currency exchange booths has decreased by 21, and 1 service center of commercial banks has been closed down.

According to NBG statistics, 67 microfinance organizations operated in Georgia and their number decreased by 15.2% yearly.

Currency exchange 1030 booths were operated annually and their number has decreased to 83.

As for commercial banks, 15 private banks were on the market, which is less by 1 in comparison with the last October. From 15 banks in 14, foreign capital is involved. They have 134 branches and 799 service centers.

Total share capital amounted to 4.861 billion lari by the end of October.

Banking Financial Market

Banking sector of Georgia is represented by 15 commercial banks; Including 14 - in the authorized capital with the participation of foreign capital. According to the National Bank of Georgia, total assets of Georgian commercial banks (in current prices) increased by 481.6 million GEL or 1.3 percent (decreased by 0.6 percent without the exchange rate) and reached 38.3 billion GEL. The banking sector's own funds amount to 4.9 billion lari, which is 12.7 percent of the total assets of commercial banks. The total share capital of banks increased by 599 million lari in 1 year.

The provision of loans to individuals has been introduced since 1st January 2019. The aim of this provision is to support stable functioning of the financial system of Georgia and to encourage healthy lending. Which will facilitate sustainable development of the economy of the country.

Regulations set out in the provisions will be simultaneously compulsory for both commercial banks and microfinance organizations, as well as for credit unions and loan issuer bodies.

Source: National Bank of Georgia: <http://nbg.gov.ge/>

Regulations will reduce the retail loan segment and it is not excluded that it will have a negative impact on the economy. The reform will be especially painful for them because self-employed people who cannot show their income, but always address such organizations.

Obviously, the simplicity of borrowing also includes risks that a financially uninformed customer can get a nonoptimal decision. Because of this fact, the NBG devotes a significant resource to rise financial education. According to the statement of construction and trade, as well as banking sector representatives, since January 1, lending rate has been significantly reduced. As a result, the demand of mortgage and other goods that used to be available to

purchase in the past, has been reduced. It is noted that due to the restrictions on issuing loans, the sale of flats in comparison to January last year has been reduced by 30%, and in some cases within the frames of 70%.

New regulations do not impede issuing "healthy credits". Statistics requires a detailed economic analysis, made by the Ministry of Economy and National Bank specialists. Failure was a problem that could have become a systemic challenge for our economy. This problem required urgent and principled steps, and the fight against insolvency cannot cause the prevention of healthy credits. When we talk about a healthy lending system we should have the most comfortable conditions created between creditors and customers,

In the end, all the financial institutions in the country that will issue a loan, whether it is a bank, a micro finance or other legal entity, must have a standard of responsible crediting and should be based on this standard. These organizations should study the creditworthiness of a borrower, his/her incomes, and most importantly, the ability to pay, how much they can afford to pay their loan. Ultimately, this will lead to reduction of risks both for the entire financial sector and in the first place for the population.

Effective functioning of the securities market plays an important role in the development of the country's economy. Developing countries experience absence of their own funds, and one of the best ways to attract investment capital is the creation of the securities market. Stock exchanges create the necessary precondition for trade in the securities market. They represent the indicators of the economic level of states.

Financial Market of Stock Exchange

In developed countries the financial market is distributed among banks, insurance companies and stock exchanges. Apart from direct investments, there are two alternative ways of business and economy development - bank loan and securities market. The first mechanism implies the entry of investors in banks as deposits in banks (for a certain percentage) and then giving credit by banks as a loan (for a higher per cent). In the case of the securities market, the cash flows directly go from the investor to the economy, in exchange for securities issued by companies or other bodies. Citizens of Georgia do not have a great choice to save money. If they have a savings or want to deposit in the bank, they have to accept a small amount of profit, or want to invest in a small business, which is very risky in most cases. In successful countries, people with free money buy shares. In case of such investment, people benefit from dividends and become prospective business co-owners. Thus, they participate in the development of the country's economy.

Today, in Georgia, the stock exchange, where permanent trading of a lot of companies should take place, is practically frozen. However, with the help of the US Government, USAID's best American experts in this field have laid the foundation for securities market in 1998-2000. The Law on Securities Market, adopted by the Parliament of Georgia in 1998, was well aware of the independent development of the above-mentioned alternative financing mechanisms (despite the banks and the National Bank's resistance). In

developed countries, they are more or less developed at the same level and have a fair share of the financial service market, since they have been formed over the centuries and have developed almost the same stages of development. Obviously, if two alternative fields are in the same situation at the initial moment (at the same level of development), natural competition among them is promoted and contributes to the increase of their efficiency; but if the starting point of one of them is at zero and the second is much better, then the normal competition will not take place and the monopolist will always try to suppress the competitor right at the starting point.

In the mentioned law, the securities industry was separated from its natural competitor - banking sector to give the newly established mechanism of the securities market a real possibility of independent development. This separation was expressed in a number of aspects: banks could not directly participate in the market (through only affiliated brokerage companies); no shareholders of the stock exchange could have had more than 10% of the stock, while banks could not have more than 50% of the stock market; the Securities Market and its participants were supervised by an independent regulator - Georgian National Securities Commission - which was a collegial management body and apart from the supervision, was called to promote this industry.

In 1998-2000, the basic infrastructure of the securities market (the Georgian Stock Exchange, the Central Deposit of Securities of Georgia, up to 12 independent Registrars) was established and started, up to 40 brokerage companies and others were established and operated. In 2000-2007, the securities market was gradually becoming stronger in Georgia. However, in 2007-2008, changes in the "Securities Market" law led to the discreditation of the securities market:

- It became possible to trade without the stock exchange, resulting in more than 95% of transactions outside the stock market, in an untransparent and non-competitive environment. This caused investors' mistrust for the securities as well as the entire market. And this, ultimately, leads to a significant decline in market liquidity.

- Independent regulator was abolished and the supervision of securities was started by the National Bank. The National Bank's priority is always commercial banks and is less interested in the development of stock exchange trade.

- Commercial banks were given the opportunity to purchase a stock exchange control package. In the end, banks own more than 50% of the stock exchange shares and the majority of votes among the decision makers in accordance with the charter. This is a good chance to carry out processes independently, in accordance with their wishes.

Due to the abovementioned, without the good will of the state it is impossible to solve these problems. Also it has to stimulate stock exchange with various methods. The same is required from the government by the Association Agreement. The Agreement does not specifically mention a stock market arrangement scheme and neither the permission of trading on stocks outside a stock exchange. EU directives consider that "Best Execution" rule means that an organizational market participant must ensure that its

clients have the best deal of transaction. Since real best conditions are provided by the transaction on the stock exchange, that is why the demand of transactions on securities only at the stock market served right for the satisfaction of these conditions.

It is also important to implement a pension reform for the development of the stock, which has already entered into force since January, 2019, and will result in a state accumulative pension system in which the large part of accumulated funds will be invested in local securities, in the local economy.

Thus, the process of establishing the securities market in developing countries has a major role for the state. The securities market is an essential and important element of the global economy, without which sustainable economic activity is impossible. It is necessary to share international experiences that include the best practice sharing and the establishment of a legal base of modern standards with the participation of a wide range of professionals. The state is obliged to support the expansion of the market participants' activities and improve services, ensure transparency, openness and organization of the securities market.

Conclusion

As the analysis has shown, the modern insurance market does not fulfill the function of providing financial market credit resources at a higher level. Improvement of the situation will only be achieved through new and existing regulations, which should focus on increasing the level of trust of the population, increasing the cost of solvency and sustainability of the insurance company, elaborating mechanisms for protection against high quality risks while performing an investment function.

In developing countries, a state is responsible for the process of establishing a securities market. The securities market is an essential and important element of the global economy, without which sustainable economic activity is

impossible. It is necessary to share international experiences that include the best practice sharing and the establishment of a legal base of modern standards with the participation of a wide range of professionals. The state is obliged to support the expansion of the market participants' activities and improve services, ensure transparency, openness and organization of the securities market.

The reforms carried out by the National Bank have been reflected in the Annual Report published by the European Commission on the fulfillment of the terms of the Association Agreement. The European Union assesses the main bank's activities positively. Regulations and regulatory acts ensure that the Microfinance Loan Market becomes more transparent and accessible, but in case a customer's interest must also be protected. It is necessary for the NBG to continue to work to ensure consumer protection in the future in order to enhance relevant mechanisms and meet the needs of financial institutions in accordance with the Eurodirections that will help to improve the quality of the financial system.

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