AMERICAN JOURNAL OF ECONOMICS AND BUSINESS MANAGEMENT

ISSN: 2576-5973
Vol. 6, No. 12, 2023

The Role of Reinsurance in Ensuring the Financial Stability of Uzbekistan Insurers

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Abstract: This article examines the problems of reinsurance in ensuring the financial stability and solvency of insurance companies in the Republic of Uzbekistan. Proposals, recommendations and conclusions have been developed on the improvement of reinsurance activities in Uzbekistan and the further development and improvement of mechanisms for improving the efficiency of reinsurance use in ensuring the financial stability of insurers.

Key words: insurance, insurance market, reinsurance, obligatory reinsurance, reinsurance contract, financial stability.

Introduction. In the years of independence, the insurance industry in Uzbekistan rose to a new level. Today, 41 insurance companies have been providing their services to policyholders on the basis of competition in the insurance market of our country. The experience of the past years shows that the government of our country have been paying attention on regularly supporting and developing insurance and reinsurance industry. In recent years, great attention has been paid to the field of reinsurance, which is an integral part of the insurance system, and a number of legal and regulatory documents have been developed by our government for this field.

According to the Law of the Republic of Uzbekistan No. LRU-730 of November 23, 2021 "On Insurance Activities", reinsurance - the risk of paying the insurance compensation (insurance payment) accepted under the insurance contract is assumed by the insurer (reinsurer) in accordance with the reinsurance contract concluded with another insurer (reinsurer) defined as full or partial insurance[1].

Literature analysis

Kh. Shennaev defined reinsurance as follows: "Reinsurance is a system of economic relations related to acceptance of risk for insurance (secondary placement of risks). In order to create a balanced insurance portfolio and ensure the financial stability of insurance operations, the insurer transfers part of the accepted risk to another insurer upon mutual agreement (secondary risk placement). In addition to reinsurance operations, specialized reinsurance companies mainly carry out reinsurance. Reinsurance takes the form of active (giving the risk) and passive (accepting the risk). In addition, reinsurance is in relative and non-relative forms[2].

[1] Law of the Republic of Uzbekistan No. LRU-730 of November 23, 2021 "On Insurance Activities"
[2] Kh.M. Shennaev, S.Shirinov "Reinsurance" E: "Economics and Finance" 2009, page 10.

ISSN 2576-5973 (online), Published by "Global Research Network LLC"
under Volume: 6 Issue: 12 in Dec-2023 https://www.grnjournals.us/index.php/AJEBM

Russian scientist Grishenko N.B defined reinsurance as follows, "The essence of reinsurance is redistribution of the obligations assumed by the insurer to cover losses under the insurance contract between two or more organizations in order to ensure the financial stability of the insurer[3].

Based on the above, we summarize the points and define reinsurance as follows: Reinsurance is a set of financial relations related to the creation of a balanced insurance portfolio and the provision of the insurer's excess of risks to another insurer under agreed terms in order to ensure the financial stability of insurers.

Research methodology

In this article, data was collected and analysed to study the topic. The results were analysed in statistical comparative methods, and the results were expressed in percentages. Based on the obtained results, a positive proposal and conclusions were given.

Analysis and results

In the middle of the 19th century, the development of industrial production in European countries increased the demand for reinsurance of a large amount of insurance risks. It was possible to expand the scope of the insurer's services, provide insurance coverage for new insurance risks only through reinsurance.

The reinsurance business provides for redistribution of risks by time and territory and provides the basis for maintaining the solvency and financial stability of direct insurers.

Reinsurance is recognized as an important factor in ensuring the financial stability of any insurance company. This practice allows companies to take huge and unpredictable risks. The purpose of reinsurance is to create a balanced insurance portfolio that ensures the financial stability of the insurance company and the profitability of insurance operations. Therefore, reinsurance protects not only insurers, but also large insured objects from financial losses, while at the same time it guarantees the state income from taxes on insurance activities. The main function of reinsurance is the transformation of risk, and as a result, the distribution of insurance obligations between several companies in domestic and foreign markets is achieved.

As a result of reinsurance, the insurer's insurance options are expanded, the ground is created for acceptance of objects that cannot be insured due to the high probability of occurrence of an insured event without fear of bankruptcy. Reinsurance allows the insurer to minimize exposure to existing risks and controls compliance with regulatory requirements. The insurer determines the share to be retained under the insurance contract at its own discretion. In the reinsurance relationship, no legal relationship arises between the insured and the reinsurer, in which the insurer and several reinsurers participate (Fig. 1).

[3] Grishchenko N.B. Fundamentals of insurance activity: Study guide. M: Finance and statistics, 2006.360 p.

ISSN 2576-5973 (online), Published by “Global Research Network LLC"
under Volume: 6 Issue: 12 in Dec-2023 https://www.grnjournals.us/index.php/AJEBM

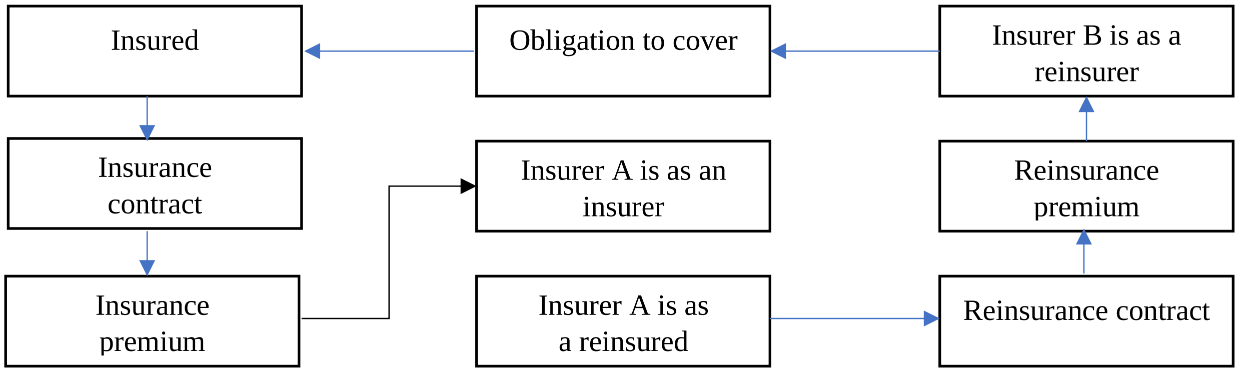

Figure 1. Reinsurance implementation process[4]

The level of use of reinsurance in the insurance market of countries with a developed insurance system is high, which can be explained by the fact that reinsurance premiums account for 40-45% of total insurance premiums, and in most countries, insurers prefer to use the obligatory form of reinsurance in order to protect themselves financially. At this point, we consider it appropriate to comment on the concept of "obligatory reinsurance". Obligatory reinsurance is a compulsory form of reinsurance, in which, according to the terms of the reinsurance contract concluded by the ceding company with the reinsurer, the risks under the main insurance contracts included in the scope of this contract are transferred to the reinsurer, and the reinsurer is obliged to accept these risks.

Obligatory reinsurance contracts can be concluded with companies that additionally deal with local reinsurance. In this case, certain types of insurance are selected, for example, construction-installation risk insurance, property insurance, cargo insurance. A certain part of the company's obligations under all contracts concluded under these types of insurance is automatically transferred to the reinsurer. In this case, an important task appears in front of the insurance company, that is to determine the amount of the share to be retained. It is necessary to solve such a task carefully, because it is important to adhere to the standards of solvency and not to damage financial stability.

In order to ensure the financial stability of the insurers, it is advisable to conclude a obligatory reinsurance agreement with local as well as foreign reinsurance companies. As a result of the implementation of this measure, the distribution of the company's losses (liabilities) between the two parties will help maintain financial stability, as well as reduce the volume of import of reinsurance services. If the structure of such a transaction with local companies ensures the preservation and distribution of reinsurance premiums in the domestic market, cooperation with foreign companies will create an inflow of reinsurance by attracting their insurance obligations.

M. I. Braginsky admits that through reinsurance, the insurer will have the opportunity to redistribute the liability between himself and the reinsurer.[5] From this point of view, reinsurance is understood as a method of risk redistribution aimed at ensuring the financial stability of insurers. The basis of the insurer's financial stability (formed authorized capital, insurance reserves and reinsurance system) represents its financial capabilities. Based on this, the financial stability of the insurance organization can be defined as its potential for obligations. The issue of ensuring financial stability requires the insurer to comply with the following conditions:

[4] Developed by the author.
[5] Braginsky M.I. Contract law. Contracts for the performance of work and the provision of services.// Monograph.-M.:statut.2002

ISSN 2576-5973 (online), Published by "Global Research Network LLC"
under Volume: 6 Issue: 12 in Dec-2023 https://www.grnjournals.us/index.php/AJEBM

- the presence of free funds in excess of obligations, with the increase in the volume of insurance operations;
- not to accept obligations beyond one's financial capabilities;
- formation of a balanced insurance portfolio by insurance amount, insurance risks, objects and territory;
- not allowing insurance coverage to exceed insurance premiums.

The mechanism of impact of reinsurance on financial stability includes:

1. Reducing the insurer's risk of damage from insurance operations. Such losses occur due to the excess of insurance premiums for a given financial year. This condition can be caused by:

a) the insurer does not have a large and balanced insurance portfolio;

b) an unexpected increase in the number of insurance incidents this year;

c) one insurance compared to the average value of previous years increase in the amount of insurance coverage corresponding to one event;

g) emergence of the need to make insurance payments under several contracts at the same time due to the catastrophic consequences of one insurance event.

2. Increase in the insurer's ability to conclude insurance contracts for a large amount of insurance. In order to ensure their financial stability and maintain their solvency, insurers have no right to conclude a contract for an amount exceeding a certain percentage of their funds. If the insurer's solvency does not allow it to assume the obligations under insurance contracts in full, it can transfer part of it to reinsurance. This is especially important in the conditions of competition in the insurance market, because the possibilities of the insurer depend on the results of its activities.

Allows insurers to regulate the ratio between the volume of their funds and the volume of insurance operations. In order to ensure financial stability, each insurer must have its own capital in the amount of not less than the specified percentage of the obligations under insurance contracts. If the size of the insurer's capital does not meet the specified requirements, it is obliged to increase its capital or reduce the size of insurance operations. It is less possible to raise the amount of capital quickly, which means that refusing to enter into new contracts or cancel existing ones leads to distrust of customers and their distance from the company. In such a situation, the transfer of a part of the insurer's obligation to reinsurance leads to a reduction in the volume of total obligations, as a result of which it is possible to fulfill the specified ratio without abandoning the conclusion of insurance contracts.

Enables insurers to more efficiently carry out operations on new types of insurance. The lack of sufficient work experience and statistical basis for calculating tariff rates in the company's activities creates a serious risk. By assuming a certain part of the obligations, reinsurers reduce its possible losses, which allows the implementation of new types of insurance on a large scale, and as a result, the development of insurance operations is achieved. Reinsurers are interested in the successful operation of their contract partners, that is, direct insurers, because the results of their activity depend on the insurers.

The use of the reinsurance mechanism is considered by most insurance companies as an additional cost, that is, the cost of sharing insurance premiums with the other party and the cost of risk transformation. Despite the regulatory requirements for the use of reinsurance, insurers do not prefer to use such a mechanism.

ISSN 2576-5973 (online), Published by "Global Research Network LLC"
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The level of reinsurance in the insurance market of countries with a developed insurance system is high, which can be explained by the fact that reinsurance premiums account for 40-45 percent of total insurance premiums.[6]

The global reinsurance market is based on the global redistribution of risks, and major catastrophes, regardless of where they occur, cause sudden changes in reinsurance prices around the world.

The role of reinsurance in ensuring the financial stability of world insurance organizations is increasing. In the reinsurance market, compared to the direct insurance market, the processes of consolidation and globalization of insurance, banking and fund capitals are more evident. Based on the need to increase the level of capitalization of reinsurers, this process provides for the formation of financial resources important for the reinsurance of natural disasters and losses estimated at several billion dollars.

It should be said about the reinsurance sector of the insurance market of Uzbekistan that today a reinsurance company that manages this sector at a professional level has not yet been established. However, with the Decree of the President of Uzbekistan[7] specific requirements for the establishment of authorised capital were defined and it has been noted that the insurance companies that have fulfilled it can carry out reinsurance operations in the prescribed manner. Insurance organizations such as "Uzbekinvest" EIIC" JSC, "KAFOLAT insurance company" JSC, "Uzagrosugurta" JSC and "Gross Insurance" JSC are operating in the reinsurance market of Uzbekistan today. The main goal of these insurers is to support the financial stability and solvency of domestic and foreign insurance companies.

Effective use of the reinsurance mechanism increases the financial potential of insurers and allows expanding the scope of activity. Unfortunately, it is necessary not only to use reinsurance, but also to rationally solve the issues of its introduction in the country's insurance market. The indicators show that the insurance companies of Uzbekistan are undercapitalized, and keeping even a part of the objects belonging to its territory in the country requires strengthening its financial foundations.

In some cases, the nature of the accepted risk in insurance organizations is not deeply studied and analyzed, but all attention is focused on increasing the size of the insurance portfolio. In our opinion, in order to further increase the role of reinsurance in ensuring the financial stability of insurance companies, it is necessary to implement the following measures:

Insurance companies should carefully develop a reinsurance strategy. In this case, it is necessary to comprehensively study the company's financial capabilities, analyze natural, political, ecological and technogenic risks, and calculate their probability of occurrence using statistical data. Also, it is advisable to focus on the nature of the risk and not on the amount of the share to be left in the company and, if necessary, to re-insure part of the liability. It is precisely as a result of not properly studying and analyzing the risk that a large amount of insurance payments can be made, which can negatively affect financial stability.

When concluding reinsurance contracts, it is expedient to introduce the procedure for payment of bonuses to the reinsured from the reinsurer's net profit. Implementation of this event is beneficial for both parties. In the contracts where the insurance event did not occur, a certain part of the reinsurance

[6] Source: Aon's Analytics Division in Reinsurance Solutions.
[7] Decree of the President of the Republic of Uzbekistan "On measures to reform the insurance market of the Republic of Uzbekistan and ensure its rapid development" dated August 2, 2019 No. 4412.

ISSN 2576-5973 (online), Published by "Global Research Network LLC"
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premium (in percentage) is returned to the reinsured at the end of the contract, and this directly motivates the insurer and automatically arouses interest in using the reinsurance mechanism.

Ensuring the financial stability of insurance companies can be achieved not only by transferring their obligations to the reinsurance company, but also by carrying out reinsurance. It is possible to increase the level of capitalization of the insurer by carrying out this practice. Establishing and expanding international cooperation in the development of the company's reinsurance activities and thereby increasing the financial stability of the company will create favorable conditions for incoming reinsurance. By transferring liabilities beyond its financial capabilities to the international insurance market, it strengthens cooperation and, as a result, accepts risks from abroad, thereby ensuring the inflow of foreign currency into the country.

Also, an important condition for companies to conduct cooperative relations with foreign countries is to be recognized by international rating agencies. This aspect is the most important indicator that attracts both foreign partners and investors. Expanding and sustaining international cooperation in reinsurance shows high performance indicators in the future.

Conclusions and suggestions

It should be noted that Reinsurance is recognized as an important factor in ensuring the financial stability of any insurance company. This practice allows companies to confidently accept very large and unpredictable risks. The purpose of reinsurance is to create a balanced insurance portfolio that ensures the financial stability of the insurance company and the profitability of insurance operations. Thus, the reinsurance mechanism financially supports the insurance company in expanding its activities, gaining a position in the market and increasing its insurance capacity.

Reinsurance allows insurance companies to increase the capacity of their insurance portfolio by concluding direct insurance contracts for risks beyond their financial capabilities. With the help of this mechanism, the insurance company will be able to maintain the necessary balance in its activity regardless of any external factors (random change of damage, occurrence of losses, losses resulting from cumulative losses). Thus, the reinsurance mechanism financially supports the insurance company in expanding its activities, gaining a position in the market and increasing its insurance capacity.

The activities of professional participants in the insurance market of Uzbekistan are not organized at a professional level, which prevents the perfect implementation of insurance and reinsurance processes.

Implementation of measures to study, analyze and apply the experience of developed countries in the reform and development of the insurance sector is considered effective. In particular, it is appropriate to use the experience of the Russian reinsurance market, which is geographically and economically and politically close to Uzbekistan, to justify the place of reinsurance in the insurance system, to determine its role in strengthening the solvency of insurance companies.

Insurers who transfer their obligations (risks) to foreign companies for the purpose of reinsurance should first submit proposals to insurance companies that have the right to carry out this practice in the country. Insurance companies make their own decision whether to accept the offer or not, and it is important to note that the terms of the offer communicated to local insurers are consistent with the terms offered to foreign companies. A domestic insurer's acceptance of the offer is considered to be beneficial in many ways, most importantly, it will reduce the outflow of capital, which will increase the potential of the reinsurance market and the investment opportunity of the insurers.

ISSN 2576-5973 (online), Published by "Global Research Network LLC"
under Volume: 6 Issue: 12 in Dec-2023 https://www.grnjournals.us/index.php/AJEBM

We believe that the implementation of the mentioned recommendations will increase the role of reinsurance in ensuring the financial stability of Uzbekistan's insurers.

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ISSN 2576-5973 (online), Published by "Global Research Network LLC"
under Volume: 6 Issue: 12 in Dec-2023 https://www.grnjournals.us/index.php/AJEBM