

# Theoretical fundamentals of the integration process of banking institutions and insurance companies of Ukraine

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Received: September 5, 2021 | Revised: September 23, 2021 | Accepted: September 30, 2021

DOI: 10.5281/zenodo.5544196

## Abstract

This article reveals the theoretical foundations of the integration process of banking institutions and insurance companies of Ukraine. The concept of “bank insurance” of own and by definition of various scientists is theoretically substantiated. It is established that the integration of banking and insurance should also be considered as a macroeconomic phenomenon, as this process in its scale and pace of development in the world already covers not only the integration relationship between individual banks and insurance companies, but also the integration of banking and insurance institutions. are participants in the financial market of a particular country. It is proved that the concept of integration of banking and insurance can be defined as the process of combining the capital of insurance companies and banks or their participation in the capital and division of resources of BSI components (management, information, technology, personnel, etc.) in the case of joint financial services. An important component of modern economic relations is the development of globalization and integration processes, which have been transformed into a powerful direction of building world economic relations, which determines the direction of social, economic and political development. It is studied that the development of international economic integration patronized the emergence of integration processes in world markets for financial services. Since the late 80's of the twentieth century. industrialized countries created conditions in the financial markets, which contributed to the mutual segmental penetration of the banking and insurance markets. Integration processes, which allow the country to join the world community (globalization), directly affect the development of the environment in the domestic market, including to ensure the interaction between the insurance and banking markets and the integration of their own benefits.

**Key words:** bancassurance, integration, integration mechanism, banking institutions, insurance companies, banking risk, crediting, bank, banking activity.

## Introduction

One of the important components of modern economic relations is the development of globalization and integration processes, which have been transformed into a powerful vector for the development of economic and political world economic relations. Promoting the country's entry into the world community, integration directly affects the development of its domestic market environment, in particular

to ensure the interaction of insurance and banking markets. Among the signs of globalization there is a tendency to form the integrity of the world as a result of market integration. Accordingly, one of the factors in the development of globalization processes in the market environment is the integration of insurance and banking markets, which ensures the emergence of interdependencies and

relationships between them and the formation of a single banking and insurance alliance.

The process of globalization of financial markets in the world economy has changed the relationship between banks and insurance companies. The mutual entry of banking and insurance business has been the dominant trend in the financial market over the past ten years, which created the preconditions for consideration and analysis of the phenomenon of bank insurance. Integration in the form of bank insurance is implemented in practice in the domestic market and has its own dynamics of development. The integration of banks and insurance companies is currently a new stage in the development of banking and insurance systems. This is due to both the expansion of activities and spheres of influence of banks, and the desire of insurance companies to increase the number of customers and, consequently, the amount of profit. Therefore, there is a need to study the best option for unification and its possible forms of achieving the above goals in the current period of economic development of Ukraine (Zharikova O., & Cherkesenko, K., 2021).

Research of problems of organizational bases of cooperation of banks and insurance companies, integration and disintegration processes in their activity, the mechanism of integration of these financial institutions in the context of interaction in the financial market was carried out by scientists-economists: R. R. Harutyunyan, T. V. Booth, A. M. Yermoshenko,

V. V. Kozyuk, L. B. Lutsiv, O. M. Malakhova, M.S. Klapkiv, Y.M. Flaps and others. At the same time, further research is needed on the development of integration of participants in the banking and insurance markets in the context of intensifying globalization processes in the world in order to solve them immediately. Banking in general is quite risky, but if you anticipate and minimize the risk, it will allow you to get a stable income. In the course of their activities, banks enter into high-risk agreements on a daily basis, which, upon their successful completion, bring banks high profits. Therefore, integration processes are considered as one of the most important problems of banks. However, the task of integration processes of banks and insurance companies remains a major issue, due to the diversity of the process, diversity of application methods, risk minimization areas, strategic areas of banks and banking products and requires further study.

**The aim of the article.** There is a scientific substantiation of theoretical and practical principles of bank insurance in Ukraine, a detailed financial and economic analysis of one of the largest banks in Ukraine JSC CB "PrivatBank" and the financial condition of its insurance partners. The study also aims to develop recommendations on ways to optimize the cooperation of banking institutions with insurance companies in Ukraine and to identify possible prospects for cooperation of the studied bank.

## Material and methods

To achieve the goal of the study, a set of general scientific methods was used. Observation and comparison methods were used to determine the analysis of a financial commercial bank. The study used a selective method, as the degree of integration of banks and insurance companies is always individual. Therefore, it is advisable for each institution to

use a representative sample of several companies. The method of mathematical processing of time series was also in the study, as it is the basis of horizontal and vertical analysis of the enterprise, assessing the value of financial condition, as well as the study of operating and financial leverage.

## Results and discussion

Being the most effective regulator of public relations, law as is designed to promote the development of integration processes, to

ensure their interaction on a parity basis taking into account the interests of both parties (Zharikova O., & Cherkesenko, K., 2021).

Ukraine's integration into the European political, economic and legal space has been proclaimed as one of the main priorities of state policy. This direction is considered in the Law of Ukraine "On Principles of Domestic and Foreign Policy" of July 1, 2010 (Pro zasady vnutrishnoii) and in Concept of implementation of the state policy in the field of informing and establishing communication with the public on topical issues of European integration of Ukraine for the period up to 2017 approved by the Cabinet of Ministers of Ukraine on March 27, 2013 (Kontseptsiia realizatsii).

Insurance is a system of economic relations between policyholders and insurers, which includes a set of forms and methods of creating trust funds (insurance funds) and their use to compensate for losses caused by various adverse events (insurance events) (Yermoshenko, A. M., 2012). Also, insurance is a system of economic relations arising from the purchase and sale of insurance coverage in the course of meeting public needs for insurance protection (Zharikova O., & Cherkesenko, K., 2021).

The banking system is a set of financial institutions aimed to comprehensively carry out operations to attract temporarily available financial resources, save individuals and legal entities and place accumulated resources on their behalf in accordance with their maturity and payment in accordance with agreements (Potapenko E. G., Kulapov V. L., 2011). The banking system organizes and diverts capital which is the main attribute of the market, ensures its attractiveness, accumulation and distribution in the social production areas with the deficit of the capital. For most domestic banks, credit risk is the primarily importance factor condition und that needs to be controlled and minimized. Credit risk is risk of default on a debt that may arise from a borrower failing to make required payments to a bank. Under economic transformation, bank insurance can be an effective method of bank's credit risk minimizing (Zharikova O., & Cherkesenko, K., 2021). The definition of "Bancassurance" is given in Table 1.

**Table 1 – The definition of "bancassurance"**

Author	Definition
<b>N.E. Avanesova</b> (Bulatova, E. V., 2004)	Bancassurance – a set of financial services that can meet both banking and insurance needs of the client concurrently
<b>V.M. Kremen'</b> (Davydenko, N. M., 2006)	involvement of banking institutions in the processes of production, marketing and distribution of insurance services.
<b>A. Slyusar, A. Bochkaryov</b> (Sliusar, A., 2006)	Bancassurance involves offering banking and insurance services and products through common distribution channels and/or for the same customer base
<b>N. Tkachenko</b> (Tkachenko, N., 2015)	Bancassurance is a service of insurance products sale through the banking network
<b>A.M. Yermoshenko</b> (Zhuravin, S. H., 2009)	The process of interaction between insurance companies and banks which results in unity and integrity of business processes related to the interests of owners, the state and consumers.
<b>O.B. Zharikova, K.I. Cherkesenko</b> (Zharikova O., & Cherkesenko, K., 2021)	Bancassurance (banking insurance group) can be understood as a long-term association of an insurance company with a banking institution in order to provide banking and insurance services within an existing or newly established banking company.

*Source: compiled by the authors based on their own research*

Thus, based on the above definitions, we can suggest our own definition of bancassurance (banking insurance group). Bancassurance can be defined as a long-term association of an insurance company with a banking institution, in

order to provide banking and insurance services within an existing or newly established banking companies.

Features of integration processes in economics:

- integration has a dual nature, it can act both as a process and as a state;
- integration is a dynamic process that can demonstrate the evolution of its types and forms of development;
- integration is characterized by the existence of interaction, interpenetration and coherence between the participants;

- integration should be regulated by the state at the legislative level (Uhryn L., 2002).

To identify the key factors (Table 2) that motivate banking institutions and insurance companies to look for ways to integrate, it is necessary to analyze the main features of these financial institutions.

**Table 2 – Criteria for deciding on cooperation between banks and insurance companies**

Banks	Insurance companies
Insurance of pledge as a real estate in their captive companies and bank risk insurance with well-known universal insurers	Reliable and well-known banks
Choosing several insurers on favorable terms	Cooperation with a small bank for pledge insurance
Cooperation with universal leading insurance market companies	Availability of a professional security service in the bank and its branches, technology for securing loans with pledge and control over transactions in case of bank risk insurance
European approach to accreditation of insurers that insure the bank pledge	Provision of insurance risks by the insurer's banking institution

*Source: compiled by the authors based on their own research*

The interaction of banking and insurance business results from the common interest in banking insurance. Banks benefit from their branches network maximum loading, branching out their traditional business areas by providing customers with a wide range of financial and insurance services, as well as receiving additional commissions for the services sale. Cooperation with banks allows the insurance company to take advantage of synergistic opportunities to use a common customer base, use the brand or reputation of the bank in banking insurance (Zharikova O., & Cherkesenko, K., 2021).

The activity areas of banks and insurance companies often intersect, which creates an objective basis for their close cooperation. Banks do not just provide clearing and cash services to policyholders, but also place their free funds, and they also are one of the largest customers of insurance companies. Insurance companies, in turn, provide insurance services to banks, as well as contribute to the creation of banking obligations.

There are several opportunities for banks to enter the insurance market. They are common for most countries and include the following:

- Greenfield;
- Mergers and acquisitions;
- Creation of a joint venture;
- Distribution agreement or strategic alliances.

In the “distribution agreement” model, the bank directly performs agency functions, i.e. it mainly acts as a sales channel for standardized insurance and investment products.

Starting a business from scratch – Greenfield – has the highest level of integration of banking and insurance capital. This model is high-cost and bears much higher risks than acquiring a company. It requires a significant amount of time spent by the banking institution top management and significant capital investment before a positive economic effect is achieved. In addition to addressing business technology issues, there is also the issue of the physical location of the new company, which requires additional capital expenditures.

If a bank intends to create an insurance company, it runs a serious risk of not achieving high performance and not concluding profitable contracts. If the bank manages to create its own customer base, the commission income from insurance services will be lower than in the

existing institution. Lack of experience in the insurance industry will negatively affect the activities in the initial period of existence. Lack of salespeople and management staff in a bank will demand for hiring new people and their retraining to work for an insurance company. The main advantage of this model of banking and insurance capital is integration is the ability of a bank or insurance company to build a financial institution from scratch, taking into account their plans for strategic development of the business and the expected characteristics.

Mergers and acquisitions are also considered a reasonable solution for banking and insurance capital integration. The advantages of this model include:

- first, coordination of activities of both institutions;
- secondly, the experience of joint activities can be applied by both the bank and the insurance company, as they make the united structure since its establishment;
- third, it is the best way to quickly enter a new business.

The main problems involve the analysis of the acquired company, its compliance with the goals and objectives of the business development strategy and the future return on investment. The unifying factor is that organizations involved in the merger process must create new value through complementarity from the merger and increase the effectiveness of joint activities.

The merger results in a larger and more comprehensively structured company with greater capabilities and prospects. The creation of a joint venture involves the formation of a new legal entity, which belongs to the parent companies – the bank and the insurance company – and is controlled by them (Zharikova O., & Cherkesenko, K., 2021). The bank and the insurance company, the bank partner, jointly build the strategy of the new company, manage it and develop the products. The factors that significantly reduce the risks of each partner are listed among the advantages of this method of capital integration. The high level of relations formalization with its detailed description of the functions of partners in the development of a

new market segment, significantly reduces the risks. Lack of need to integrate the management structures of the partners into a single mechanism allows to maintain a high level of project management.

The disadvantages of the method include a significant level of initial implementation costs. One of the main risks of this method of integration is that the bank bears the risk of income and reputation loss. The practice of mergers and acquisitions of banks and insurance companies indicates an increase in the financial potential of newly established financial intermediaries. The interaction of banks with non-bank financial intermediaries in the establishment of financial supermarkets contributes to the strategic goal of every successful financial intermediary. The goal implies providing comprehensive financial services at a high level and to obtain synergies through combining their competitive advantages.

Development of a mechanism for the integration of insurance companies with banks requires identifying key starting points for integration and its forms interpretation, as well as the constituent subsystems of this mechanism (Fig. 1).

“Mechanism of insurance companies and banks integration” involves a set of subsystems, including the principles and forms of integration, the tools for the integration management, as well as tools for integration risks management, which operate on the basis of interdependent relationships and aim to achieve unity and integrity inside the systems.

The basis of insurance companies and banks integration is made by financial convergence in the global financial services markets, which has led to the establishment of financial conglomerates as a form of heterogeneous integration processes between insurers and banks when a financial association is managed by a financial institution and a loan institution is an element of the insurance market, i.e. one participant of the integration belongs to the insurance field and the other – to the banking.

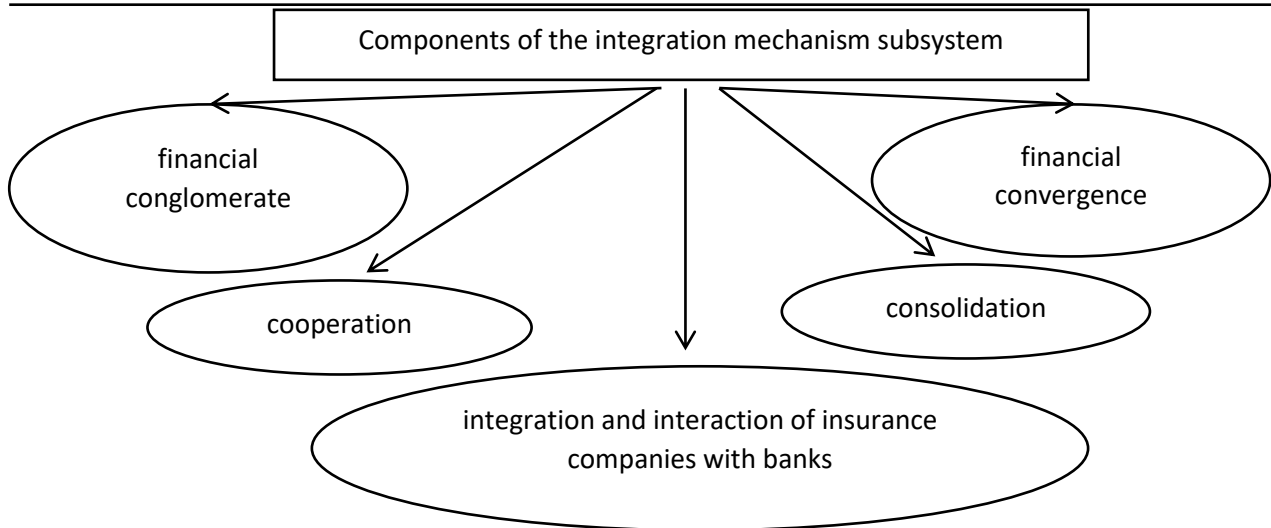


Figure 1 – Subsystems of banks and insurance company’s integration mechanism

*Source: compiled by the authors based on their own research*

The processes of integration of two financial institutions taking place in industrialized countries’ developed financial markets in the field of banking and insurance are mainly manifested in two trends – integration, expressed by the concept of “co-financing”, and disintegration, which is outlined in the concept

(Zharikova O., & Cherkesenko, K., 2021). A comprehensive analysis of scientific approaches to studying the problems of integration allowed to develop a classification of the main elements of banking and insurance institutions integration (Fig. 2).

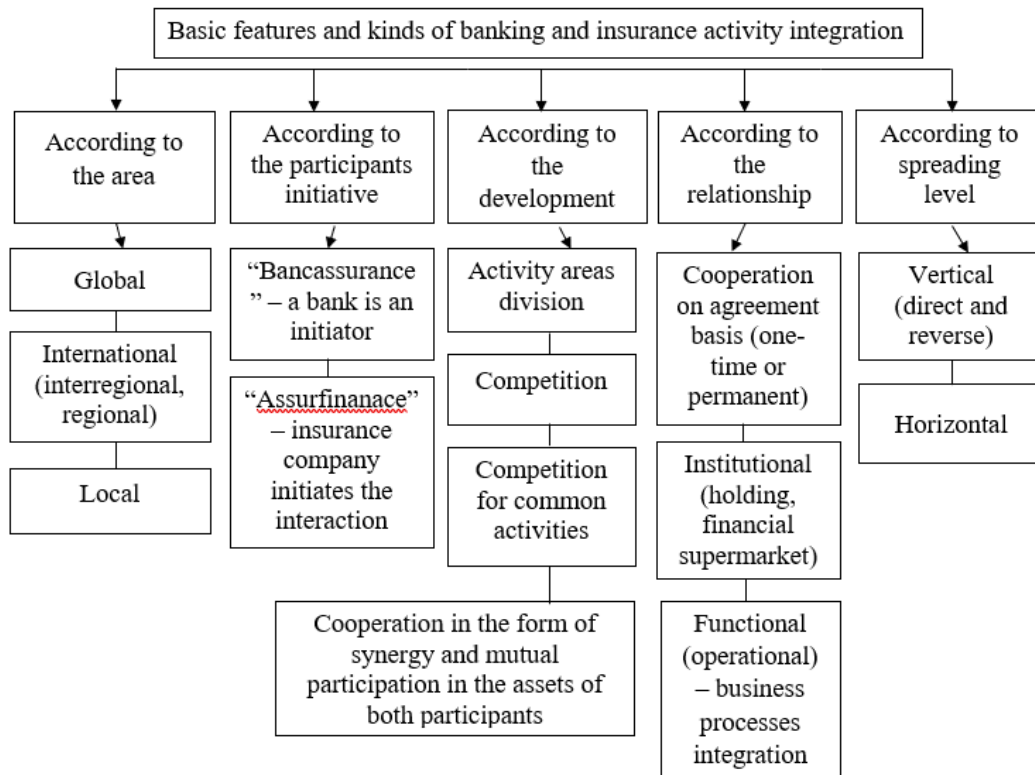


Figure 2 – Classification of banks and insurance companies integration

*Source: compiled by the authors based on their own research*



Stages of institutional integration development:

The first stage involves the organization of cooperation between banks and insurance companies on the agreement basis. This cooperation can be one-time or permanent. Further development of integration processes in the activities of financial intermediaries results in the need for new institutions, i.e. the combination of market positions of banks and insurance companies in the initial phase leads to the concentration of financial capital and the creation of new financial structures – financial groups and holding companies, financial supermarkets and others.

The second stage of the organization of relations between banks and insurance companies involves their operational integration, the essence of which is reflected in offering both specific banking and insurance products and joint banking and insurance services to the customer. Vertical integration should imply the integration of technologically interconnected business processes based on the provision of joint services within a single financial intermediary on an

economic basis. This integration is intra-organizational and can be considered as a process of achieving the unity of capabilities of all departments.

Horizontal integration is used at the initial stage of development of interaction between banks and insurance companies, it implies organization of joint activities at the divisional level of the bank or insurance company. For example, the bank's credit departments study and take the possibility of interaction with the insurance company to prevent credit risks. Departments of the insurance company, which implement financial risk insurance schemes, also study possible areas of interaction with banks (Reverchuk, S. K., Syva, T. V., Kubiv, S. I., Vovchak, O. D., 2005). Based on this concept, there is no "integration mechanism", and the notion of the concept is used to analyze the process of interaction of insurance companies with banks, i.e. a set of subsystems that include principles and forms of integration, integration management tools and integration risk management tools based on interdependent relationships and aimed at achieving unity and integrity in the system.

## Conclusions

The analysis shows that bank insurance in Ukraine has significant prospects for development, due to the interest of banks in additional sources of commission income and the desire of the insurer to increase sales of insurance products. The simplest forms of bank insurance related to the sale of related financial products, which are the most common. The economic integration of banks and insurance companies has no specific definition, but is based on the common idea of all scholars on this concept, namely the merger of two or more financial institutions or at the macroeconomic level to increase operating profits, market impact and efficiency.

JSC CB "PrivatBank" occupies a leading position in all financial and economic indicators of the industry and the confidence of the population, as it serves a third of household deposits and more than 24% of the population of Ukraine.

The example of JSC CB "PrivatBank" shows that banking insurance technologies occupy an important place in the current phase of

development of the domestic financial segment. Due to a significant customer base and a wide network of branches, the income from the sale of insurance products in 2020 is almost 16% of the total income of the bank, as the volume of bank insurance in «PrivatBank» is growing quite rapidly. According to the study, PrivatBank can also be recommended to find new partners for cooperation between leading companies such as AXA Insurance and Providna. In conclusion, we consider it appropriate to interpret the financial supermarket as the highest form of integration of business processes of banking institutions and pension funds, mortgage funds, insurance, investment funds and other institutions that provide financial services to meet customer needs. The advantage for the customer when implementing the concept of "financial supermarket" is the purchase of a full package of services in the office, saving time and money at the same time.

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