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INSURANCE OF COMMERCIAL BANKS' CREDIT FACILITIES AND CREDIT RISK MANAGEMENT

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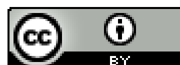
Abstract: The practice of insurance of credit facilities of commercial banks is an important means of credit risk management in banking activities. Through insurance, banks can protect their loan portfolio from risks and reduce losses related to customers who face default or other debt situations. Development of diversified insurance products, automation of processes by introduction of technological solutions and use of international experiences are considered important for improvement of insurance practice. These approaches are of great importance in reducing credit risks and making banks more efficient. This is it in the article commerce of banks credit objects insurance to do practice improvement and on prudent credit risk management approaches and international experience analysis will be done

Keywords: Credit facilities, insurance, insurance companies, credit risk, risk management, insurance, damage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Introduction

Credit objects insurance do business banks for mandatory remedy it is credit of operations risk to decrease and debt of recipients payment ability negative effect showing cases banks protection to do directed. Today's in the day insurance system improvement necessity increased is going because insurance companies and banks between cooperation credit risks more efficient to manage demand does.

The bank's credit activity is one of the main criteria that distinguishes it from other non-banking organizations. In world practice, a large part of the bank's profit is related to lending. At the same time, non-repayment of loans, mainly large loans, can cause the bank to break.

One of the issues of proper organization of banks' activities and minimization of existing risks is to determine and analyze credit risks, their quality and level.

As the economic development moves to a new stage, the problem of bank risk management is renewed, and the research in this regard is also improving . The reason for this is that the problem of risks and its management is updated with the development of the digital economy and is becoming an urgent problem in the banks' activities.

Based on the above points, the credit policy is the strategy and tactics of the bank in the field of credit portfolio management, organized on the basis of a set of predetermined rules and solutions for lending in order to ensure the safety, liquidity and profitability of the bank by reducing credit risks. Each bank can develop and conduct its credit policy independently, taking into account political,

economic, organizational and other factors.

Literature review

Improving the practice of insurance of credit facilities in commercial banks involves enhancing credit risk management strategies. Effective management is crucial for minimizing potential losses and ensuring financial stability.

Establishing Sound Lending Principles

- Commercial banks should implement robust lending principles that guide credit decisions, ensuring that loans are granted based on thorough assessments of borrowers' creditworthiness (Kwabena, 2014) .
- Risk management committees must oversee the establishment of policies and guidelines tailored to specific industry standards, which can help mitigate risks associated with various financial instruments (Kwabena, 2014).

Utilizing Predictive Models

- Developing predictive models for assessing credit risk can significantly enhance decision-making processes. For instance, factor analysis can be employed to evaluate the risk levels of retail clients, allowing banks to tailor their lending strategies accordingly (Konovalova et al., 2016) .
- This approach not only aids in identifying high-risk borrowers but also facilitates the creation of internal credit ratings, which can streamline risk management practices (Konovalova et al., 2016)

Continuous Improvement and Adaptation

- Regular financial analysis and adaptation of credit risk management practices are essential. Identifying shortcomings in existing systems allows banks to implement targeted improvements, thereby reducing credit risk exposure ("Improving credit risk management in a commercial bank", 2023).
- The integration of international best practices into local banking strategies can further enhance the effectiveness of credit risk management (Kenjaev, 2020) (Karimov, Temirkhanova, 2020).

While these strategies can significantly improve credit risk management, it is also important to recognize that external economic factors and regulatory changes can impact the effectiveness of these practices. Continuous monitoring and adaptation to the evolving financial landscape are necessary for sustained success.

Inefficient risk management is reflected in high concentration of one borrower, short-sighted lending policy, and weak control over the activities of important personnel. It should be taken into account that the above situations occur in all countries, including the banking activities of developed countries (Bessis, 2015).

Methods

Economic research methods were used to systematically analyze the data using a systematic approach to studying the problem.

The methodological basis of the research is formal logic, statistical and comparative analysis methods, systematization, classification and expert assessment, grouping, comparative method and content analysis, graphic interpretation methods, etc.

Result and Discussion

face a number of risks in the process of lending. Defaults on loans, natural disasters or other emergencies increase credit risks. Therefore, banks cooperate with insurance companies and offer insurance products in order to reduce the risks related to the solvency of borrowers (Golinelli and Morici, 2021). Loan insurance allows the bank to outsource certain risks through an insurance company, which reduces losses associated with loan coverage.

Commercial banks usually insure the following credit facilities:

- Collateral properties for mortgage loans;

- Vehicles for auto loans;
- Property and other assets for other loans.

Loan insurance allows the bank to work with high-risk segments, which increases the bank's profit and expands the range of customers (Chesney and Stoffels, 2020). In addition, insurance activities ensure continuity of liquidity for the bank and prevent losses.

Credit risk is closely related to banking activity, in which the borrower cannot fulfill his obligations to return the principal amount of the loan and to pay the interest calculated on it under the conditions specified in the loan agreement. Credit risk means that the borrower may delay or fail to make payments on the debt, which in turn may cause problems in the bank's cash flow and adversely affect the bank's liquidity. Despite innovations in the financial services sector, credit risk remains a major cause of banking problems. More than 80 percent of bank balance sheets are focused on this aspect of risk management. There are 3 main forms of credit risk:

- Personal or consumer risk;
- Corporate risk or company risk;
- Sovereign or country risk.

It is important to conduct a comprehensive analysis of the bank's ability to evaluate, manage, monitor, control, implement and repay loans, bonds, guarantees and other credit instruments for the existence of potentially dangerous consequences of credit risk.

Credit risk is defined as non-fulfillment of the terms of the loan agreement by the borrower, that is, non-payment of the loan amount (in part or in full) and the interest on it within the terms specified in the agreement. Therefore, identification and management of credit risks is an integral part of any commercial bank's strategy to achieve its development and growth goals.

Credit risk management is the basis for the survival of most banks. An overview of credit risk management, including an analysis of banking policies and practices. This analysis should determine the adequacy of the financial information provided by the borrower used by the bank in making a decision on granting a loan to the borrower. Since risks are variable, the risk for each loan should be periodically reassessed.

The main elements of credit risk management are as follows:

- Credit portfolio management;
- Credit function and credit operations;
- Credit portfolio quality;
- Dormant (non-earning) loan portfolio;
- Credit risk management policy;
- Credit risk limitation policy;
- Asset classification;

Loan Loss Provisioning Policy.

The actual problem of credit risk for banks is that in the presence of credit risk, the creditor (bank) lacks confidence in the borrower's ability to fulfill the terms of the loan agreement and his obligations at the specified time. It is known that the profit in banking practice consists mainly of interest on loans. A decrease in the bank's profit due to non-payment of the interest rate or principal amount of the loan on time or not at all on the loans received by the borrower leads to a decrease in the weight of the bank's future funds. Therefore, lenders try to reduce the risks associated with the return of the funds they provide.

The level of existing risks in the borrower's activity can be determined before the creditor grants the loan, later after the loan is granted, and during its use. In order to minimize the risk, the lender tries to identify the risk before granting the loan.

Credit risk can be caused by the following situations:

a) various macroeconomic and microeconomic factors, changes in economic legislation and norms;
b) changes in the economic and political environment in the borrower's activities, the cash flow suitable for repaying the loan due to adverse events inability to organize;

c) lack of full confidence in the value and quality of collateral received for securing the loan;
d) lack of highly educated bank employees and customers;
e) loss of reputation of the borrowing entity at the local or state level, changes in its business activity, etc.

In a credit relationship, lenders expect that the amount loaned or borrowed will be repaid on time and that the intended interest rates will be received at the specified time. They avoid risk, are interested in the level of risk associated with it before giving a loan, determine it and accept a positive conclusion on granting a loan in cases where the level of risk is minimal for them. But the result expected by the creditor may not always be what he thinks.

Banks and bankers should be more risk averse than other lenders. The reason for this is that the bank does not work with its own funds in relation to other creditors, but with borrowed funds, that is, with the funds of individuals and legal entities that are temporarily in the bank. The ability of the bank to give credit depends on the resources it has attracted. The bank, in turn, should be able to return these funds to the client when required. This opportunity requires timely identification of existing risks in the bank's activity and the development of measures to prevent them.

If we look at the scheme of the crediting process of a commercial bank, it is possible to estimate the level of risk on the loan given at the stage of determining the creditworthiness of the client.

Credit risks and their level can be determined at each stage of the lending process. Although the level of risk related to the creditworthiness of the client is not present or is low in the initial stages of lending, the emergence of unexpected financial difficulties during its activity may be the basis for the emergence of credit risk.

The emergence of credit risk depends on two main parameters, the extent to which the lender and the borrower fulfill their duties. Analyzing the loan package prepared by the borrower and preparing a loan project provides an opportunity for the lending bank to determine the risk and its types. At this stage, the lender:

1. The borrower's economic and financial situation, his work ethic, moral image, production capabilities, marketing, financial management, etc.;
2. How well-founded the request for credit is and whether this basis is based on the true economic situation of the enterprise.

Questions such as whether the purpose of the loan is in the interest of the bank should be fully and clearly answered. For example, in the current stages of the market economy, new enterprises and firms are being established and they It is very important to answer the first question in the absence of accurate information.

The second question must be filled out by the borrower, its financial situation, the state of its calculations, reports and conclusions on audits, enterprise balance sheet, cash flow report, income statement and other information necessary for the bank, and the presence of these documents indicates the success of the enterprise's own financial resources. may indicate that he is driving.

In the third question, the bank should determine whether the loan it is giving corresponds to its loan portfolio or not. If this lending leads to greater diversification of the bank's loan portfolio, it will reduce the risk of the bank's loan portfolio. The risk of the loan portfolio may increase if this loan increases the lending to the same sector, and the repayment period coincides. In this case, whether the bank employees have sufficient knowledge in the field of lending and credit evaluation, if they are not accepted by the market, they should be considered responsible for the credit evaluation process.

1. Application for a loan.
2. Assessing the creditworthiness of the client and the efficiency of the loan.
3. Loan agreement, pledge, guarantee agreement, loan insurance.
4. Giving credit.
5. Monitoring the use of credit.

6. The loan and the interest on it are paid on time.
7. There will be difficulties in paying loans and interest.

Several general stages can be distinguished in the credit risk management process of a commercial bank. These are: developing the goals and objectives of the bank's credit policy; organization of the administrative decision-making system and credit risk management administrative structure; analysis of the debtor's financial situation; determine the debtor's credit history, his connections; drawing up and signing a loan agreement; analysis of the risk of non-repayment of loans; establishing and maintaining credit monitoring of the borrower for all loan portfolios; implementation of activities related to repayment of overdue and doubtful loans and sale of collateral, etc.

In order to manage the credit risk, the bank employee must constantly monitor the quality and structure of the loan portfolio. As part of the "profitability-risk" debate, the bank employee is obliged to limit the rate of profit while avoiding excessive risks. It should implement a risk sharing policy and avoid the accumulation of loans in a few large debtors. Otherwise, the inability of one of the borrowers to pay the loan can complicate the financial situation of the bank.

Credit risk can lead to liquidity risk and the risk of bank insolvency, as well as risks related to the bank's inability to cover administrative and economic costs. Although interest rate risk is independent in itself, it can deepen the chain of credit risk and all other risks.

One of the urgent problems of commercial banks is credit risk management based on balance sheet data and loan portfolio analysis. Grouping loans into risk classes, analyzing them, developing methods to minimize them and protect the bank's interest reduces credit risks. Avoiding the accumulation of credit in enterprises and sectors whose production is decreasing, as well as following the saying of the sages that "one should not put all eggs in one basket", observing the maximum amount of risk per borrower allows to reduce the credit risk.

Grouping loans by risk classes is 1/5 (20.66%) of all bank loans allows to conclude that it is above or in the normal risk zone. This is a significant figure for a single bank. This amount was mainly due to the existence of overdue loans. The given classification is useful because it defines the amount of loans in the risky zone and thus encourages bank employees to pay special attention to this particular loan and minimize credit risk.

Property received as security for a loan - this is the last source of loan recovery.

One of the important indicators in determining the level of credit risk is the coefficient representing the financial independence of the enterprise.

Currently, most of the commercial banks of our republic do not thoroughly analyze the value of the loan when giving loans. The price set by commercial banks for loans - currently consists of the following elements: based on the refinancing rate of the Central Bank of the Republic of Uzbekistan, banks determine the price of the loan without additional calculations.

In countries with a highly developed market economy, the market price of the loan is used as a basis for determining the price of the loan. Calculating the price of the loan to the client consists of several stages, and this indicator is analyzed by commercial banks. The main goal of determining the price of the loan is to achieve the efficiency of the loan given by the bank, to achieve profit and ensure the bank's liquidity. This result is to prevent bank risks in advance can identify and prevent them.

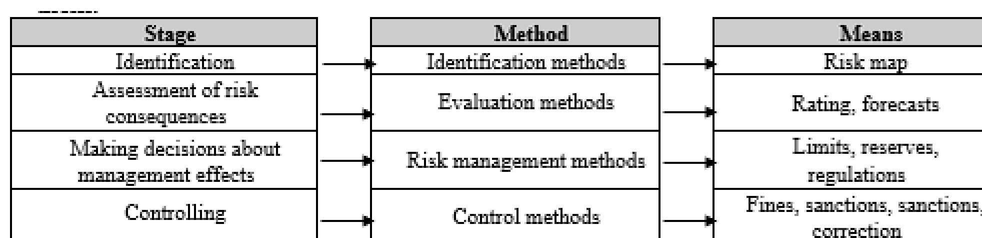

Fig. 1. Bank risk management methodology
Source: Compiled by the authors.

In addition, it is desirable to develop the process of risk management in banking activities

based on a clear methodology. In this case, the methodology of risk management in banking is as follows (Fig. 1).

First of all, it is necessary to determine the stages of risk management in commercial banks. At the first stage, the risks that may occur in the bank's activity are determined, that is, they are identified. In the second step, the likely consequences of the risks are assessed. At the third stage, a decision is made on the impact of management on risk prevention. And finally, in the fourth stage, the implementation of the decision is controlled.

In addition, the methods of risk management that occur in the activity of commercial banks should be fully expressed in the banking risk management methodology. Such methods include identification methods, assessment methods, risk position management methods, and control methods.

The stability and competitiveness of commercial banks depends on the proper organization of their resources and their rational use. It should be noted that there are a number of unsolved problems in the field of organization, management and diversification of the deposit and loan portfolio of commercial banks

Conclusion

It should be noted that the lower the level of risks, the higher the probability of profit. Therefore, every commercial bank should try to choose the minimum level of risk among alternative solutions.

Risks directly affect commercial banks' financial indicators, including liquidity and solvency indicators. Therefore, based on the relevance of the issue of developing interest rate risk management methodology in commercial banks, our study focused on the issue of interest rate risk management by commercial banks on a scientific basis, showing its main stages and the applied mathematical apparatus, due to its conciseness in modern banking practice and the availability of a wide range of experts. we recommended extensive use of the assessment method.

Having studied foreign experience in risk management, we were able to make the following suggestions:

1) commercial banks in developed countries have special specialists for all types of risks. Statistical and expert analysis of risks is appropriate;
2) in the system of risks, which are divided into pure and speculative risks, financial risks should be insured as they are characteristic of speculative risks;
3) in the classification of risks, systematic and unsystematic are distinguished, and if systematic risk is observed in cases of decline in bank activity as a result of changes that lead to various financial changes, unsystematic risk is explained by the deterioration of the financial situation as a result of the influence of factors related to the bank, and it is necessary for the bank to conduct marketing research in this direction:
4) increase the level of information provision of economic activities as the main ways of reducing risks; moderation of financial expenses; risk insurance; methods such as diversification of capital investments and expansion of the type of activity are used;

The main noteworthy point of practice of 5) is that they have created an effective system of economic and legal risk management, that is, managers can pre-evaluate the origin of financial risks during the financing process and determine measures for their optimization.

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