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BANKING RISKS IN THE CONTEXT OF THE FINANCIAL CRISIS 2008

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Abstract:

This article examines the major risks facing banks in the current financial crisis and how banks have changed their approach to risk assessment and management. The financial crisis of 2008 and the bankruptcy of the LTCM hedge fund highlighted the seriousness of the "too big to fail" problem in financial markets. The assistance that was provided to the largest banks and insurance companies in the United States in 2008 and in subsequent years demonstrated to the largest banks that, due to their systemic importance, they can count on government support in case of financial problems, which further increased the "risk appetite" of these banks, which is clearly seen in the example of a large position on derivatives, which were occupied by these banks as of the end of 2016. The value of the derivatives position in the two largest banks exceeds the value of assets by 30 times, and in some other American banks by 200 times, which increases the risks and makes it possible to implement the financial crisis in the worst-case scenario. New conditions of functioning of financial markets make it necessary to search for new approaches to understanding systemic risk and its regulation.

Keywords: bank risks, financial crisis, assessment, diversification, stress-testing, risk management.

INTRODUCTION

Theoretical aspects of banking risks

Risk is a historical and economic category. As a historical category, risk is a possible danger realized by a person. It shows that risk is historically associated with all the courses of social development.

Banking involves risk. Moreover, banking risks are primarily caused by the need for commercial banks to fulfill the fundamental principles of their activities. The leading principle in the work of commercial banks in the conditions of market relations is the desire to make a big profit. But the pattern is that the more profit, the higher the risk.

It is impossible for the bank to completely avoid the risk. It should be about managing risks and minimizing them.

In the economic dictionary edited by Raisberg B.A., bank risk is understood as "possible losses due to adverse events, both independent and dependent on the bank's activities."[1]

In the financial and credit dictionary edited by Mamyrov N. K., bank risk is interpreted as "the danger of the occurrence of unpredictable and undesirable consequences for the bank of its own actions" [2]. A group of authors Plotnitsyn A.A., Cherkasova V.E. bank risk is understood as “specific losses in any limited area of activity of a commercial bank.” [2]

Russian researcher Grabovaya S.A., notes that bank risk is ”the possibility of losses arising from the specifics of banking operations” carried out by credit institutions [3]. But the specification of the “unprofitable” definition of bank risk is given in its classification by spheres of occurrence. The risk is almost everywhere. It turns out that the definition of risk as a possible loss is tautological.

According to Kozlovskaya E.A., banking risk is understood as “a set of interrelated various risks (credit, interest, liquidity, and so on)” [4]. This definition shows the structure of banking risks.

Another approach to determining bank risks is carried out through the probability of deviation from the necessary. This approach brings us closer to understanding the essence of risk. This opinion is shared by Professor V.T. Sevruk [5] Firstly, probability is a quantitative characteristic of the degree of possibility of an event. Secondly, each probability corresponds to a strictly defined value of the outcome. Thirdly, the risk situation is characterized by a probability distribution according to certain distribution laws. The latter is of great practical importance; it allows you to establish the probability of a relationship from the expected income. Moreover, deviations can be positive and negative. In the first case, we are talking about the chances of making a profit, and only in the second - the risks. Therefore, the considered approach can be modernized and the risk can be defined not just as the probability of deviation, but as the probability of a negative deviation of reality from the expected.

The considered approach to risk as a statistical characteristic is one of the most common in modern

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economic literature. L. Harris in "Monetary Theory" notes that "the share of any proper portfolio with specific probability distributions of income, the average standard deviation is by no means the only measure of profitability." However, Tobin S. showed that several assumptions are quite sufficient (if the assumptions are justified) to consider the expected income as a measure of profitability, and the standard ratio as a measure of risk.

As can be seen, there is no complete identification of risk with a statistical value. The statistical value is only a measure of risk. In this case, this measure measures the degree of uncertainty of the decision-making situation, characterized by uncertainty of information. Accordingly, "bank risk is nothing more than a situation generated by the uncertainty of the information used by the bank for management and decision-making, and characterized by a strict dependence between the possible outcome of the decision and the corresponding probability. The loss, as well as the excess profit, results from the uncertainty of the situation." [6]

Kazakh scientist Seitkasimov G. S. in the work "Banking", defines risk as "the danger or possibility of bank losses, upon the occurrence of certain events" [7]. It touches upon the concept of risk in banking practice. The risk is expressed by the probability of obtaining such non-thematic results as loss of profit and losses due to non-payments on loans issued, reduction of the resource base, making payments on off-balance sheet transactions. But at the same time, the lower the risk level, the lower the probability of getting a high profit.

Therefore, on the one hand, any manufacturer tries to minimize the degree of risk and from several alternative solutions always chooses the one at which the level of risk is minimal, on the other hand, it is necessary to choose the optimal ratio of the market level and the degree of business activity, profitability.

Banking risks in the context of the financial crisis in Russia in 2008-2009.

The activities of commercial banks, as well as other financial and non-financial institutions, are always fraught with risks. Risk in banking is commonly understood as the possibility of financial losses and loss of liquidity associated with internal and external factors affecting the bank's activities. Risks are realized as a result of non-compliance of forecasts with actual developing events. Accordingly, the phenomenon of risk is associated with the uncertainty of the latter and always exists in a situation of uncertainty regarding changes. The degree of risk reflects the level of probability of loss of expected profit or capital as a result of an unpredictable change in circumstances. Quantitative and qualitative risk assessment is important, which is associated with determining the level and identifying risk factors. The need to measure risks is caused by the need to determine their acceptable level, which can be adopted in the management of banking activities.

The global financial crisis that broke out in 2008 revealed significant shortcomings in bank risk management, showing the importance of building a reliable and effective risk management system. At the same time, it is very characteristic that the modern financial crisis began precisely in the banking sector, where risk management systems have always been sufficiently developed and have been the subject of serious control by society in the person of state and banking supervision and regulation bodies, as well as by international banking institutions. Obviously, the problem lies not in the absence of bank risk management as such, but in its compliance with the new realities of the economic environment of banking activity. From this point of view, the lessons of the modern financial crisis are subject to the most in-depth analysis and generalization.

As the experience of most countries has shown, crisis phenomena, developing incrementally, passed through several stages. The first stage of the crisis in all countries was somehow connected with a crisis of confidence, banks stopped lending to each other, the outflow of money from the banking sector began. The second stage was characterized not only by problems of liquidity and interbank lending, but also solvency, when due to a lack of funds, banks could not fulfill their obligations to customers in a timely manner. The inevitable consequence of the growing problems in the banking sector in all countries covered by the crisis was problems with the availability of bank loans for enterprises and the population. The inability for borrowers to re-credit led to defaults and a sharp deterioration in the quality of banks' loan portfolios. This stage of the crisis development, when it began to cover other sectors of the economy in addition to the financial sphere, was called the asset crisis, which is characteristic of the third phase of the global financial crisis. A distinctive feature of the fourth phase of the crisis, in which banks of all developed countries found themselves, was the capital crisis. At this stage, the risk of lowering the capitalization of banks and violations of regulations tied to the amount of capital has increased sharply due to borrowers' defaults.

For each of the selected stages, which have their own specific features, certain types of banking risks are characteristic, which become especially relevant and critical in certain periods of time.

In Russia, at the initial stage of the development of the financial crisis, namely in the autumn of 2008, liquidity risk and market risks were the most relevant for the banking system. The aggravation of liquidity problems in the activity of banks at this stage was due to the imbalance of financial assets and liabilities of credit institutions. As a result, the Russian banking system was unable to withstand the liquidity squeeze, when a rapid

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outflow of capital from the country began and interest rates rose, and only some banks had access to extraordinary sources of financing. Despite the severity of the problems associated with the liquidity crisis, its peak phase in Russia and other countries, as a rule, is quickly overcome, the key to which is the active assistance of the state. However, even now many banks still continue to experience difficulties with attracting resources, and the liquidity risk and the subsequent inability of the credit institution to ensure the fulfillment of its obligations in full remains relevant.

Market risks, the level of which is always high in banking, have already been largely realized at the first stage of the crisis development. This is as distinctive a feature of this stage as the increase in liquidity problems. It should be emphasized that market risk is caused both by the uncertainty of fluctuations in market conditions and by the sensitivity of the system to these fluctuations. Losses of a credit institution arise as a result of unfavorable changes in the market value of financial instruments of the trading portfolio and derivative financial instruments, as well as the exchange rates of foreign currencies and precious metals.

Market risks include, as is well known, stock, currency and interest rate risks. Since currency risk is accompanied by losses due to exchange rate changes in an unfavorable direction, sharp fluctuations in exchange rates pose a considerable danger for banks. Stock risk threatens losses associated with changes in the market value of securities in the bank's portfolio. During the financial crisis, periods of increased volatility in the stock market become characteristic, which leads to a significant decrease in the value of trading portfolios of securities. The risk of a change in the exchange rate of securities is associated with an inverse relationship between the rate of interest and the rate of securities: with an increase in interest rates, the exchange value of securities decreases and vice versa. This creates big problems for the investment departments of banks, since when the economic situation changes, there is often a need to mobilize liquidity and it is necessary to sell securities at a loss. An increase in interest rates reduces the market price of previously issued securities, and issues with maximum maturities usually undergo the largest price drop. Moreover, periods of rising interest rates are usually marked by an increase in demand for loans. And since the main priority of the bank is the issuance of a loan, many securities must be sold in order to obtain cash for loans. Negative exchange rate differences arising on the bank's balance sheet reduce profits. A bank that has bought securities in conditions of falling demand for credit and relatively low interest rates, i.e. at a high exchange rate, is forced to sell them at increased interest rates and a fall in the exchange rate value of securities. Such sales often bring significant capital losses, which the bank seeks to compensate for due to a relatively higher yield on loans issued.

As a rule, the market value of securities and the income of a commercial bank from them are inversely dependent: when the prices of securities are low, the income from them is high, and vice versa. Therefore, investors, buying securities during a period of low interest rates and other rates, risk facing the fact of a decrease in the market value of securities in the event of an increase in their rates. However, if interest rates decrease, the market value of securities will increase. Consequently, the increase in interest rates on securities has both positive and negative sides. New investments of funds can bring a higher income to a commercial bank, but higher rates on securities mean a depreciation of the investment portfolio of the same bank.

The profitability of certain types of securities due to fluctuations in interest rates, as a rule, depends on their maturity. The shorter the maturity of a security, the more stable its market value, the longer the term, the more the price of the security is subject to fluctuations. The negative difference in prices depending on the maturity of securities makes it possible to understand why short-term securities are more attractive to commercial banks than long-term ones. Banks adhere to a special strategy to neutralize the adverse effects of changes in interest rates. For this purpose, for example, securities are purchased, the redemption period of which fits into the predicted phases of the business cycle. If interest rates are relatively high and a phase of economic recovery is coming, the bank can start buying long-term bonds, counting on an appreciation and receiving positive exchange rate differences in the event of a fall in the rate of interest. In recent years, a greater number of instruments for hedging interest rate risk have appeared. These include financial futures contracts, option contracts, interest rate swaps, etc. It is also necessary to take into account interest rate risk, i.e. the risk of losses due to changes in interest rates on assets or liabilities of a credit institution.

It should be noted that at the second stage, the liquidity crisis is transformed into a solvency crisis. Currently, the most dangerous risk for the banking system in terms of the probability and severity of the consequences is credit risk, when losses arise as a result of late or incomplete fulfillment by the debtor of financial obligations to the credit institution in accordance with the terms of the contract. During the crisis, the probability of default of individual corporate borrower’s increases, the quality of the consumer loan portfolio deteriorates, which increases the risk of non-repayment of loans received. The dynamics of overdue debt testifies to a serious deterioration in the quality of loan portfolios: if for the whole of 2007 the volume of overdue loans increased by 52%, then in 2008 the increase was about 129%. At the same time, the growth rate of overdue debts of legal entities reached 163%. The share of overdue debt in the

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corporate portfolio (as of 01.03.09) was at the level of 3.1%, in the retail portfolio – at the level of 4.1%. At the same time, a number of experts believe that the real level of overdue debt of banks may already be 10% [8].

It is obvious that the probability of this risk has increased markedly recently, three groups of explanatory reasons can be distinguished. The first group of reasons is related to the crisis of trust. One of the consequences of the global financial crisis is the outflow of foreign investments from Russia. As a result, banks that actively used foreign borrowed funds began to experience acute liquidity problems. In addition, there was a significant decline in quotations of Russian securities. The resulting liquidity crisis led to serious disruptions in the MBC and REPO markets, which, in turn, affected the ability of banks to issue new loans. The second group of reasons is due to the close interdependence of specialized business systems, when the destruction of one of the links causes failures in the entire chain (the "domino principle"). In recent years, the process of deep specialization of business has intensified, which has led to dependence on many suppliers and consumers. Financial instability, for example, the inability to re-credit one of the links in the production chain, increases the credit risk of all participants in the process. The third group of reasons is associated with a drop in demand. The global financial crisis has already led to a reduction in production, a drop in wages and incomes, which has turned into a squeeze in demand. Despite the efforts of many companies to reduce costs, there is overstocking, a decrease in business profitability and the ability to service loans. The "scissors effect", i.e. a large credit burden and a drop in company revenue, leads to an increase in credit risk.

Due to falling incomes of the population and mass layoffs in the consumer lending sector, the level of credit risks is also increasing. The solvency of customers is falling, and banks are forced to revise their risk policy. During the crisis, it is extremely difficult to predict the ratio of "bad" and "good" borrowers, since in conditions of uncertainty and unfavorable macroeconomic situation, even clients who have confirmed their solvency may find themselves in the ranks of debtors. As a result, banks can no longer count on compensating for the risks associated with potential defaulters by paying "good" customers, as it was before the crisis. The share of credit risk in the bank's overall risk system is quite large, therefore, the severity of the consequences of this type of risk is maximal.

At the third stage, the crisis of liquidity and solvency is transformed into an economic crisis, covering, in addition to financial, other areas of the national economy. A characteristic feature of this stage is the asset crisis. In addition, the reputational risk or the risk of loss of business reputation is aggravated as one of the most dangerous, having irreversible consequences for a credit institution during a crisis. Since the financial stability of individual credit institutions was questioned, there was a sharp narrowing of the customer base. In this regard, the risk of loss of business reputation has increased – the risk of losses for a credit institution as a result of a decrease in the number of customers (counterparties) due to the formation of a negative perception in the company about the financial stability of a credit institution, the quality of its services or the nature of its activities in general. Banks with a significant share of retail business, actively attracting funds from individuals, are most affected by reputational risks. Restructuring of credit institutions experiencing financial difficulties with their subsequent absorption by state-controlled banks should not lead to the dominance of state ownership in the financial sector.

The fourth stage of the crisis is characterized by the process of lowering the level of capitalization of banks. It should be noted that the capitalization crisis is currently the most urgent for banks in all countries. Currently, the need for Russian banks to recapitalize has increased. Due to the sharp increase in overdue debt, banks are forced to form an increased amount of reserves for possible loan losses. In February 2009, amendments to the law "On Banks and Banking Activities" came into force, which oblige banks by 2010. increase the volume of own funds to 90 million rubles, and by 2012 – up to 180 million rubles. Currently, the standard of adequacy of own funds – HI – for most of the largest banks is held quite high. In particular, it exceeds 14% in more than 60 organizations [9]. At the same time, it should be borne in mind that the quality of banks' own funds is declining. Thus, the ratio of second-tier capital to first-tier capital in many Russian banks is close to the maximum. In Russia, the government has proposed a program under which banks that have already received subordinated loans from Vnesheconombank will have more attractive conditions for replenishing capital. In particular, for every ruble invested by a shareholder, the state adds three rubles. Previously, the ratio of 1 was valid for all participants of the program:1. Having received support, the bank is obliged to issue loans to companies and citizens in at least the same amount.

The head of the US Treasury Timothy Geithner believes that most American banks that have passed stress testing are able to replenish capital without the help of the state. The volume of necessary additional capitalization, revealed by stress tests, amounted to $ 75 billion. USA [10].

In a crisis, risk management issues become key. In Russia, an effective banking risk management system is at the stage of formation and includes mechanisms for institutional regulation of banking activities at the macro, meso and micro levels. At the macro level, the main regulators of systemic risk in the banking sector include restrictions on the composition of bank portfolios, state insurance, the amount of liability for bank obligations, etc.

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Volume-19, February-2023
ISSN: 2749-3601

Within the framework of the banking system itself (meso-level), regulatory acts of state supervision bodies and standards act as regulators of banking risks. Supranational structures include the Basel Committee on Banking Supervision. At the meso-level, in order to optimize banking risks, institutional regulation mechanisms are being formed, in particular, the minimum amount of capital for newly created banks, bank capital adequacy standards, liquidity standards, standards for the organization and operation of internal control services, etc. are being established. At the micro level, additional mechanisms for managing banking risks are used, certain risk assessment methods and models are used. The main task of risk management is to protect the interests of the bank by maintaining the necessary level of reliability and risk optimization. The risk management system, as a rule, is entrusted with the functions of identification, assessment, risk optimization and conflict of interest resolution. Identification of the bank's risks in a financial crisis can be carried out according to the risk map, in which, firstly, the main risks of the bank in the current situation are identified, secondly, basic risk management measures are developed, and thirdly, the departments responsible for their implementation are determined.

The expected risk during a crisis is equal to the weighted sum of all possible risks in the activities of commercial banks multiplied by the probability that these risks are realized. The increase in the probability of realization of each of the considered types of risks in a certain period of time is associated both with the general economic development of the country and with the positions of a particular bank.

In a crisis, risk management is aimed at optimizing them, while it is necessary to identify not only the types of risks, but also the periods of occurrence of unpleasant events, as well as possible scenarios for the development of the situation. The intersection of these axes of three-dimensional space (views, time, scenarios) forms an ordered set of information blocks, the analysis of which is important for decision-making. The range of risks is universal for commercial banks, however, each bank takes its own risk positions in a crisis. In addition, the crisis could not but affect the risk assessment methodologies used by banks. In order to reduce credit risk, banks are forced to take a more careful approach to the choice of customers, tightening the rules for assessing borrowers. In terms of assessing the financial situation of the borrower in a crisis, the role of an individual assessment against a formalized one is significantly increased. During the evaluation, special attention is paid to the latest (current) information about the financial situation of the client, the role of liquidity indicators, turnover and debt burden increases. However, in the new conditions, a problem is found due to the fact that the timing of receipt of new (up-to-date) information about the financial condition of counterparties does not correspond to the speed of development of the financial crisis. In such conditions, one of the main tools of work is a thorough knowledge of the client and the specifics of his business, as well as well-established long-term relationships with him, allowing you to get information before the market.

The tightening of the credit policy leads to an increase in the "cut-off level" of customers and, inevitably, to a decrease in lending volumes, which in the long term contributes to the formation of higher-quality loan portfolios.

Some risks, in particular those related to the state of global financial markets, are almost impossible to predict even with sufficient information. Therefore, a number of experts believe that the diversification of portfolios and instruments is a key element of financial security, allowing to minimize the losses of the organization in any event. Many credit institutions have already adjusted a number of investment limits for certain types of financial assets, as well as revised the list of their counterparties.

Risk assessment is also complicated by problems that already existed in our country. It should be noted that there is no culture of disclosure of financial and business information among domestic companies: there are no standards for the preparation of consolidated financial statements, legislation regarding the regulation of the issue of disclosure of owners is incomplete. The credit rating system is not developed: the legislative framework is incomplete and there are virtually no reputable national rating agencies. The limited financial market infrastructure also complicates the objective assessment of financial risks.

During the crisis, banks are increasingly using a conservative approach to risk assessment and are forced to abandon high-risk investments and operations, from long-term investments. In the current conditions, the role of stress testing and backtesting of applied models is increasing, which contributes to the actualization of the risk assessment methodologies used. The financial coefficients used to assess the financial position of the borrower are adjusted taking into account the results of stress testing.

Classical approaches to risk management in a crisis do not give an objective and adequate result. Therefore, it is necessary to shift the emphasis from formal quantitative assessments to expert assessments and judgments, which, in turn, requires a high level of competence and professionalism of risk managers.

The current crisis has shown that most banks have put on stream risk assessments on financial instruments that other financial institutions and regulatory authorities have demonstrated confidence in. To a lesser extent, those banks that supplemented standard approaches with their own models and independent estimates were shaken. This proves that, along with risk management, it is advisable to

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manage the uncertainty that forms the sources of risk. Unfortunately, the approach based on the management of risk sources described in the literature is poorly used in practice. Experts believe that "the use of this method can give a significant advantage to companies in conditions of increasing uncertainty, reduce losses and reduce the unjustified risk rate to acceptable limits" [11].

In conditions of crisis and economic instability, the results of the implementation of certain strategies can be completely unpredictable. In this regard, it is necessary to distinguish between two groups of risks: firstly, expected, management models of which are described in sufficient detail; secondly, unexpected risks, approaches to identification and assessment of which are less developed. Special attention should be paid to this type of risks during the financial crisis, since they are in the zone of less predictable (including statistical) losses.

Different types of risks imply different approaches to their management. Optimization of expected and statistically predictable risks is based on the management of results, for example, losses, if the consequences are associated with certain losses. In commercial banks, a system of measures is provided for risk management of this kind, in particular, the creation of reserves, the formation of capital at a sufficient level is recommended, scoring models of decision-making, ORP, management of the payment position, limiting and sharing responsibility for the operation, etc. are proposed. The loss management method is widely used in commercial banks. The development of risk management methods within this approach is carried out in accordance with the requirements of the Central Bank of the Russian Federation set out in the Regulation on the Procedure for the Formation of Reserves by credit institutions for possible losses on ships, on loan and equivalent debt No. 254-P dated March 26, 2004, the Regulation on the procedure for the formation of reserves for possible losses No. 283-P dated March 20, 2006.

In the context of the financial crisis, the importance of the second approach increases, which is associated with increased uncertainty and, unlike the first, is based on the management of risk sources. Some authors suggest using economic capital to cover these risks, while others believe that in addition to this, it is important to analyze possible sources and risk factors that it is advisable to focus regulatory measures on. It may be necessary to change the business model or the structure of the customer base before the risk is committed, instead of managing losses [11].

The mechanisms of risk management in conditions of uncertainty are considered in some documents of the Basel Committee on Banking Supervision, whose task is to introduce uniform standards for regulating banking systems of different states [12]. Forward-looking assessments and analysis of possible consequences of events make it possible to develop a system of preventive measures and reduce the amount of losses. To manage the sources of risks of a commercial bank in conditions of uncertainty, it is necessary to assess potential threats, determine the sensitivity of various areas of banking activity to risk factors based on the analysis of the mutual influence of risks on each other. The development of scenarios for the possible development of events and the calculation of the probability of the implementation of each of the options will allow us to develop a system of measures aimed at optimizing the risks of banking activities in conditions of uncertainty.

The financial recovery of the banking system will be facilitated by the development of a risk-sharing mechanism between credit institutions and a Deposit Insurance Agency that would have the right to repurchase and further administer distressed assets. Government interventions in the stock market at the expense of the Federal Budget will have a short-term effect. Their impact on financial stabilization can be both positive and negative. Without any doubt, such a measure will contribute to "stabilizing market expectations and restoring the fair price of shares of domestic issuers" [13]. However, there is a risk of distortion of the market price of shares, which will lead to inadequate capitalization of individual companies and distortion of market signals.

In order to prevent systemic risks, international experts pay attention to the expediency of regulating financial institutions and instruments, as well as strengthening macroprudential supervision. According to the participants of the London G20 summit, it is necessary to strengthen financial supervision and regulation, in particular in the registration of hedge funds or their managers, as well as to provide for mandatory disclosure of information that would allow assessing risks. An important priority of d vadtsatka is the restoration of the borrowing market. In particular, financial injections are supposed to be able to support liquidity, capitalize banks and solve the problem of "bad" assets [14]. The G20 meeting participants are convinced of the need to expand international cooperation, including the introduction of supervisory boards, the institutional strengthening of the Financial Stability Forum (FSF) and the launch of a program of measures to prevent crises at early stages within the framework of the FSF and the International Monetary Fund. Financial regulation can partially weaken the cyclical nature of economic development and create prerequisites for recovery from the crisis.

Conclusion

In conditions of uncertainty and instability of the economy, banking risks are always high. It is unknown whether organizations receiving bank loans will be able to maintain planned production volumes and recoup the invested funds, and, accordingly, pay for loans.

The global financial crisis of 2008 was the most

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destructive in terms of economic indicators in the entire history of economic crises. But according to the principle of "there is no silver lining", one of the consequences of the global financial crisis was a shift in the priorities of the financial and banking community towards financial stability and the development of requirements for credit institutions that contribute to improving their financial stability.

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