**Convergence of the financial services industry in imperfectly**

**competitive financial market**

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Abstract

What is wrong with the theoretical display of demand creation and consumer choice of financial services? The answer is the assumption that we surely know prices, income and other variables that take place in that circumstances. But, in reality, the subjects have to choose and make decisions under conditions of uncertainty. In practice that is "solved" with the convergence and regulation of financial services.

Convergence as a feature of globalization has strongly affected the sector of financial services. In that sense, banking companies, insurance companies and other investment financial institutions are functionally directed toward mutual cooperation.

In this paper we understand financial convergence in accordance to the recommendations of the OECD as a term for all forms of mutual relations of banks and insurance companies as providers of financial services on the one hand, and the applicants for all types of financial products, on the other side.

Initially we perceive the levels of convergence between banks and insurance companies: 1) the level of products, 2) the level of financing, 3) the level of investment, 4) the level of financial products distribution, 5) institutional level and 6) the regulatory level. That opens space to form two theses: 1) whether the business in banking and insurance fully merged or it further remains different and 2) whether the regulation should be the same or different (special) for banks and insurance institutions.

In addition, regulation of insurance companies and in banking is analyzed by its two aspects: 1) internal supervision, which has microeconomic character and has a goal to provide corporate risks management in a frames of financial corporation operations and 2) regulation by specific regulatory bodies which has a macroeconomic character and is associated with macroeconomic goals such as: monetary stability, growth and development, etc.

*Key words:* demand, asymmetric information, convergence, financial services, risk, regulation

**Demand, consumer choice in a field of financial services, risk**

**and asymmetric information**

The theory of consumer choice seeks to uncover and explain the factors that determine the consumers behavior (in this case of financial services). Modern economics considered that the theory of consumer choice stems from four basic assumptions that in the same time can be determined as fundamental elements that explain the behavior of the consumers:

* First, among the various available financial services (monetary or insurance), the consumer who has limited income, always choose those services that maximize his own pleasure;
* Second, the taste of the consumer allows him to classify, evaluate and combine various financial services (to save, to undertake currency and interest risk from savings, to ensure the savings by forming financial portfolio or to insure savings); (Enterprises and individuals take loans for investments in business or for building houses and are planning to pay them using their future incomes. Incomes in the future are unsure, because the profit or wages in the next period may increase but they may decrease too. It is also possible business bankruptcy or the individual to remain jobless. In any case, making decisions is risk connected. The assumption here is that the subjects has an ability to calculate the risk perfectly and to remove it completely in the frames o their choice and preferences for financial products on financial markets. Later we will see that in accordance of the theory of asymmetric information that is not always like that. The difference is that here we are talking about savings and insurance in direction of maximization of the consumer surplus, and later more we will talk about savings or insurance in a sense of uncertainty of the risk – and all in accordance with probability, expected value and risk propensity).
* Third, the consumer has a given and a limited income;
* Fourth, the prices of financial services that can be purchased are previously given and known.

Budgetary constraints are limiting to the consumer packages that consumers can afford. The consumer buys packages of financial service 1 and financial service 2. The more he purchases a service 1, the less of service 2 can afford. The set of all possible scales (combinations) that accurately depleting a consumer income at a given market price is called the line of the budget. (Figure no. 1.)

**Figure 1. Budget constraints of the financial services consumer**

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Preferences are variations (individual satisfaction or benefit) of the consumer which allow him to rank the possible combinations of financial services within a given income and prices of those goods and services. Consumer shares his budget under the influence of his preferences.

The economic theory takes four simple features of comparing consumer preferences which allow him to divide the budget:

* *completeness*, which allows the consumer to rank all possible combinations of financial services;
* *"as more as better"*, assumes that the services are desirable, and that in the case of two same services, better is that one that can be easily find;
* *transitivity* means that if you want service A more than service B, and service B more than service C, then certainly you will want more the service A that service C. Also, if A is equally attractive as B, and B as C, follows that A is equally attractive as C;
* *convexity* implies a mix of financial services that are more preferred than the extremes (risk diversification).

Consumer preferences allow him to make choices between different packages of financial services (monetary or insurance).

Indifference curve is a curve that shows the consumer packages that provide the consumer the same level of satisfaction. That curve is a set of combinations that are equally attractive.

Figure no.2 shows two of many indifference curves of the consumer. The consumer is indifferent between combinations A, B and C, because they are all located on the same curve. Predictably, if the consumption of insurance services of the consumer is reduced, as an example from point A to point B, the consumption of banking services must be increased in order to remain the satisfaction of the consumer. If consumption of insurance slipped back from point B to point C, the quantity of used bank services must again be increased.

**Figure 2. Preferences and indifference curves of the financial services consumer**

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Slope at each point of the indifference curve is equal to the rate for which the consumer is willing to replace one good for another. This rate is called the *marginal rate of substitution* (MRS). It can be noted that because the indifference curves are not straight lines, the limit rate of substitution is not equal at all points on a given indifference curve. The rate for which the consumer is willing to exchange one service to another depends on the quantity of services that he/she already uses. That means, the rate for which the consumer is willing to exchange insurance for savings or credit depends on whether he is more willing to be insured or more saves (or use credit for investments), which in turn depends on his willingness to accept risk and his desire for savings or investment.

What is wrong with this theoretical review for demand creation and consumer choice of financial services? The answer is our assumption that prices, income and other variables we know for sure. But, in reality the subjects have to choose and make decisions under conditions of uncertainty. That means they have to calculate probability of events occurrence or to face the risks in decision making. In that sense an action for risk reduction have to be taken – i.e. risk diversification ("Do not put all eggs in same basket"), insurance and appraisal of the value of the right information.

We all know that in a market economy all these activities can be made to the financial markets. But the problem occurs immediately - financial markets are not perfectly competitive, which means that there is asymmetric information, so there is a problem in market signaling.

Asymmetric information is one of the essential segments emphasizes the importance of financial intermediation. Epitomized by *negative selection* and *moral hazard* as a lack of information before and after the transaction, asymmetric information is a factor for more significantly greater relative share of indirect financing of the economy. Intermediary or indirect financing, which involves the activities of financial intermediaries is more important than the direct funding, i.e. the collection of funds directly from lenders in financial markets (Mishkin S. Frederic, 2006, 171). Asymmetric information is an essential element that determines the financial structure, and analysis on how the problems of asymmetric information affect economic behavior is so called *agency theory*.

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| **Type of intermediary** | **Value of assets** **(billion $, end of the year)** |
| 1970 | 1980 | 1990 | 2002 | 2008 | 2009 | 2010 | 2011 | 2012 |
| **Deposit Institutions (banks)** |  |
| Commercial banks | 517 | 1.481 | 3.334 | 7.161 | 13.417 | 13.419 | 13.582 | 14.693 | 15.058 |
| Credit unions | 18 | 67 | 215 | 553 | 814 | 792 | 871 | 906 | 959 |
| **Contractual savings institutions** |  |
| Life Insurance Companies | 201 | 464 | 1.367 | 3.269 | 4.411 | 4.824 | 5.176 | 5.340 | 5.613 |
| Companies for non-life insurance | 50 | 182 | 533 | 894 | 1.287 | 1.377 | 1.374 | 1.396 | 1.445 |
| Pension funds (private) | 112 | 504 | 1.629 | 3.531 | 4.595 | 5.443 | 6.143 | 6.302 | 6.636 |
| State and local pension funds | 60 | 197 | 737 | 1.895 | 2.311 | 2.722 | 2.949 | 2.873 | 3.194 |
| **Investment intermediaries** |  |
| Financial companies | 64 | 205 | 610 | 1.165 | 1.912 | 1.663 | 1.630 | 1.610 | 1.534 |
| Investment funds | 47 | 70 | 654 | 3.419 | 5.274 | 6.921 | 7.873 | 7.871 | 9.324 |
| Investment funds on market | 0 | 76 | 498 | 2.106 | 3.757 | 3.259 | 2.755 | 2.643 | 2.650 |

***Table 1. Major financial intermediaries and value of their assets***

*Adjusted according to Z.1 Financial Accounts of the United States*

**(**http**://**[www.federalreserve.gov/release/Z1/LevelTables](http://www.federalreserve.gov/release/Z1/LevelTables); <http://www.federalreserve.gov/releases/z1/current/annuals/a2005-2012.pdf>**)**

Through it sets up the thesis of influencing of the negative selection on the financial structure through so-called *problem of blemish* or buying *"cat in a sack".* Due to the inability of individual investors to establish a clear distinction between good companies in which they would invest with high expected profits and low risk and bad companies with small expected profit from investment and high risk, they would pay only the price of securities reflects the average quality. Having in mind that the companies that make the securities offer have very precise information about its operations versus investors, those that work well will not want to sell their securities at an average price which means their understatement, and on the market they will offer only securities whose individual value is below average, i.e. those overrated. Individual investors realize that these are securities with poor quality and decide not to invest in them, leading to limited efficiency of financial markets.

The second major segment of asymmetric information refers to as moral hazard dilemma of choosing between debt and equity contracts, i.e. determines the choice of the company about whether to come up for additional funds through debt or through equity deals. Moral hazard as a problem of asymmetric information which occurs after the execution of financial transaction also answers some questions that determine the financial structure and indicates the importance of financial intermediation and state regulation of financial markets and the importance of collateral in debt contracts. The basic problem of asymmetric information on investments in equity securities known as *principal - agent problem* stems from the separation of the management and control from the ownership of the company. Namely, if the managers are owners of an insignificant part of the company they work for, they are actually agents of the owners i.e. of the shareholders (principals) who own most of the company. That such a separation leads to moral hazard so that managers (agents) that control operations can happen to act in accordance with their interests and not for the interests of owners of shares (principals) and be less motivated to increase profits than owners of the company i.e. major shareholders. This problem arises only because the owners do not have any information about the intentions of the managers and cannot prevent unnecessary costs or defraud, i.e. stems from the existence of asymmetric information. Moral hazard exercises its influence on a market debt securities also, and thus on a structure of the market of debts and on a financial structure in general. Given that debt securities are contractually determined to carry fixed interest and repayment of a principal value for a specified period, the borrower keeps the profits that eventually would have achieved with their venture, and it motivates them to take riskier investment projects than lenders would like. The ability to fail invested assets due to the high risk taken by the borrower or the possibility that he achieve high profit from his risky investment (where the lender has not any extra bonus unless previously agreed fixed interest), discourages the lenders in a possible greater involvement in these markets.

The existence of asymmetric information on financial markets that are causing problems of negative selection and moral hazard obviously reduces the efficiency of the functioning of those markets. In the multiplicity of possible solutions to solve those problems can be stated: private collection and selling information, state regulatory measures that lead to the increase of information on financial markets, emphasizing the importance of collateral and net value in debt contracts, establishment of restrictive clauses in contracts, etc. The overall findings of these events and movements in world practice suggest the conclusion that they lead to increasing the role of financial intermediaries in financing activities of business entities. Bellow follows a systematic review of the problems of asymmetric information and possibilities for solving them as a moment that significantly determines the structure of financing the economy.

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| **Problem of asymmetric information**  | **Possible solutions**  | **Answer of the question No.**  |
| **Negative selection**  | * Private collection and selling information
* Government regulatory measures to increase information
* Financial Intermediation
* Collateral and net value
 | 1,253,4,67 |
| **Moral hazard in ownership relations (principal – agent problem)** | * Gathering information: monitoring
* Government regulatory measures to increase information
* Financial Intermediation
* Debt Contracts
 | 1531 |
| **Moral hazard in debt contracts**  | * Net value
* Setting up and implementation of restrictive clauses
* Financial Intermediation
 | 83,4 |
| **List of questions or statements:**1. **Stocks are not the most important external source of funding.**
2. **Securities traded are not the main source of funding.**
3. **Indirect financing is more important than direct funding.**
4. **Banks are the most important external source of funds.**
5. **The financial system is strictly regulated.**
6. **Only large, well-known companies have access to securities markets.**
7. **Collateral in debt contracts is paramount.**
8. **Debt contracts have numerous restrictive clauses.**
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***Table 2. Problems of asymmetric information and possibilities for their solution* (**Mishkin S. Frederic, 2006, 187**)**

Therefore in practice there is a process of convergence of specific areas of the financial industry - that is the way to relative asymmetric information and they have microeconomic character, and are caused by costs, revenues and profits of the entities of the financial markets. On the other hand, the state wants to relative asymmetric information and doing that by the regulation of financial entities operation and financial markets operations. Therefore, below we talk about convergence of the financial services industry.

**Convergence of the financial services industry and the impact**

**of insurance and banking**

Convergence as a feature of globalization has strongly affected the sector of financial services. Functionally, banking companies, insurance companies and investment institutions are directed to cooperation. The process of convergence flattens the work of supervisory entities in the relevant financial sectors, it is getting closer and common, but it does not mean that they should merge. Business in the financial services industry remains fundamentally different in certain sectors, therefore the solution lies in promoting the integration of supervisory bodies within the separate financial sectors internationally, which will allow coordination of cooperation at national and international level.

Here we will take financial convergence into consideration under the recommendations of the OECD as a general term for all types of mutual relations of financial providers and applicants of all types of financial products and services. Convergence occurs at several levels: 1) at the level of products, 2) at the level of funding, 3) at the level of investment, 4) at the level of distribution of financial products; 5) at the institutional level and 6) at the regulatory level (Bebear, C., 2002, 45-65).

At the *product level* we see that banks and insurance companies offer more and more competitive products, and the question is only when these differences in products in banks and insurance institutions will disappear. For example, even life insurance in the household sector was taking a form of savings, as banks do with deposits.

At the *financial level*, it is easy to recognize that financial markets play the role of space for expanding the activities of banks and insurance companies. Before all, they give more flexibility and liquidity for core businesses of banks and insurance companies. Financial markets allow development of the process of securitization, for the banking credits and for the insurance policies too – helping them in a liquidity maintaining.

At the *level of investment*, financial markets and asset management are becoming strategically important for both - banks and insurance companies. In particular, insurance companies recently developed a very active investment strategies based on the optimal portfolio strategy, unlike previous times when they have invested their financial reserves exclusively in government bonds. This kind of changed behavior was determined by the requirement for financial risk support on the side of the assets in the balance sheets of insurance companies. By investing more assets in stocks insurance companies enables risk sharing and extracting more value from their assets. Thus, the behavior of insurance companies become close to that of banks in relation to monitoring the aggregate risk caused by the fluctuations in financial markets.

At the *level of distribution*, banking networks are being used more and more as channels for distributing the products of insurance companies. For example in France, 60% of the distribution of life insurance and 8% of non-life insurance goes through banks.

At the *institutional level*, convergence is very well known and can be seen in public. In recent years we have seen the appearance of broad financial conglomerates formed by different types of financial institutions: banks, insurance companies and investment institutions.

At the *regulatory level*, regulators and supervisors are confronted with very similar or identical questions and answers in insurance, banking and investment activities. In all three sectors they want to protect users of financial services, prescribing similar standards for supervision of companies, regardless of their sector of activities: a) complete information and transparency for products sold by companies, b) risk diversification in order to reduce the possibility of concentrating the risk c) coverage of assets with liabilities and so on.

However, contrary to the above convergence between financial services, business remains basically different, especially between banks and insurance companies.

The first difference is that banks generally face financial risks (market risk, liquidity risk and credit risk) while insurance companies face with widespread real risk (insurance of life, health, property, personal and commercial risk) unified with financial risk (transferred via short time gap between payment of premium and loss event). So, the specifics of insurance lie in the concentration of risk on the side of liabilities in the balance sheet, while the concentration of occurred risks in the banks is on the asset side of the balance sheet.

The second difference is that, unlike insurance, banks create liquidity on their assets. Money for lending comes primarily from deposits. In other words, funds invested by economic agents are needed copy for lending that expands to those economic agents or their borrowers, i.e. on that way we have monetary creation. Insurance companies do not create money, they just transfer money that already exist and are enabled by policyholders. Duties of insurers, in a form of paid premiums of policyholders, are used to cover possible losses or for their financial investing.

A third difference is that the insurance sector proves to be weaker source for system risk (i.e. risk of infectious liquidity risk), than the banking sector for several reasons. First, the liquidity that insurers injected into the economic system is a transfer that results from the earlier creation of value of the policyholders, unlike the liquidity which banks pumped into the economy and which is not the content of previously created value. Consequently, the market failure of the insurance company has a potential impact only on the policyholders, while the insolvency of the bank has a potential impact of a vast number of individuals, not just to its customers, which will follow the flap. Second, deposit owners in banks can raise their deposits from banks at which time they want, or after the insurance without any penalty for it, unlike policyholders that with some difficulties and with higher costs can break the contract of insurance.

All previously stated does not mention that the regulation in terms of globalization is complex. Today, three possible solutions are actual: 1) solution promoted by the French authorities about the existence of different sectoral regulatory bodies, but close to each other as they could learn and have benefit from different experiences, 2) solution promoted by the European Commission for establishment of new supervisory level based on close and confidential cooperation between supervisors (European Union member countries from the beginning of the Integration formation in 1957 started with formation of the common market for insurance, in a frame of the agreement for free flow of people, goods, services and capital, in a intension for fully elimination of all possible barriers. However, the real liberalization of insurance started with so called White paper in 1985 and its political consequences, The Unique European contract from 1986.), and 3) establishing a single regulatory body competent for the three financial sectors, whose proponents are Great Britain, Germany, Netherlands, Switzerland, USA and Japan.

As for countries in transition, globalization affects segments of the financial system but it is a different level of complexity of structure as compared to developed countries, and also within the group of transient economies. The same goes for the regulation of the elements of the financial system.

The formation of different types of non-banking financial institutions increases the level of financial intermediation in the national economies of these countries. By creating a more complex structure of the financial systems of transitory countries, there is the need for a new approach in the implementation of the regulatory function i.e. introduction of consolidated supervision. Namely, it is pronounced the trend of formation of banking groups and financial holding companies with participation of non-bank financial institutions. Independent exercise of supervisory function by specified regulatory bodies (e.g. supervision of capital market, supervision of insurance companies, supervision of investment and pension funds, bank supervision) within their scope often complicates the work. Hence, effective execution of the regulatory function of all segments of the financial services industry, involves the establishment of good cooperation between separate regulatory bodies, based primarily on information exchange and implementation of the joint supervisory controls – i.e. making framework for consolidated supervision.

**Insurance of business risks in the financial services industry using**

**financial market instruments**

The problem of complexity of the financial market where the convergence partially tries to ignore the risk by combining financial products, on a microeconomic level is resolved through financial derivatives.

In every national economy, financial system represents an area in which there is a trading with free financial funds. What actually happens is an exchange of financial resources that are aimed at bridging the time gap between current and future spending of the funds. From that kind of trading there is a benefit for the surplus subjects, whose incomes exceed their current expenditures, and also for the subjects who are deficient, whose incomes are less than their current costs. As surplus or as deficient economic subjects may be entities from all sectors in the economy – householders, corporations, state.

The structure of the financial market contains of several types of entities that act on it. These globally can be divided to: 1) primary financial entities and 2) secondary financial entities.

Primary financial entities are composed of enterprises, population, state and international corporations.

Secondary financial entities are composed of numerous financial institutions as intermediaries on the financial market, and they are known by the name financial intermediates.

Feature of financial institutions is that their basic potential is financial instruments. Core business of financial institutions is concentrated on posture and operations with financial instruments. Basic financial institutions are banks and credit funds (other financial institutions).

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Financial institutions collect funds (concentrate them) in the form of deposits, as deposits on transaction accounts, by taking loans, by issuance of securities, by buying capital share, by payment of fees, by selling insurance policies etc. Those collected financial funds financial institutions are placed in the form of loans, in a form of buying securities on financial market, or by investing in real investment projects. With those operations, most financial institutions appear as financially intermediaries.

 Separate sectors of national economy use different instruments in realizing their international financial transactions. All these instruments may differ according to the term (short-term, medium-term and long-term), according to their marketability (some can be sold on financial markets and some not), and according to the currency that follows (some are denominated in domestic currency and some not). Table 3 shows the main instruments for international financial transactions in major sectors of the national economy.

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| Domestic economy sectors  | Instruments of the financial transaction  |
| Enterprises  | - trade loans from foreign supplier - bank loans and credits- trade securities- bills of exchange and bonds- loans from foreign affiliates- stocks |
| Banks, insurance companies, and other financial institutions  | - deposits of foreign residents- trade securities- bills of exchange and bonds - loans from affiliates - stocks- insurance policies  |
| State | - treasury bills - bills of exchange and long-term bonds - inter-state loans- interstate economic help- Loans from international financialorganizations – IMF, World bank (IBRD), Bank for international settlement (BIS), and other  |

***Table 3. Financial instruments***

Enterprises enter into fiduciary-debtor relations with foreign companies, and in certain situations and with foreign banks. Economic entities issue some trade securities, which in interaction with banks turn into instruments of international payments (letters of credit, remittances, etc.). Banks and other financial institutions dealing with the collection of foreign capital using various forms (deposits, financial and credit arrangements, etc.) which are in a function of export and import of commercial entities. Governments and national authorities are financially involved indirectly through banks. They also used several forms of financial transactions in their relations with foreign countries.

Just in terms of innovation in financial markets, securities which are traded receive categorization of simple and derivative securities. *Simple Securities* offered earnings based only on the status of its issuer (interest on bonds or dividends on the shares in accordance with the profitability and solvency of the issuer). In spite of them, *derivative securities* depend on additional factors relating to prices of other assets that in fact they are based on (the payment of stock options in dependence of the price of basic stock pack, etc.).

The term financial derivative is a *general expression for securities that are derived from other securities, or securities which value is determined by the value of other securities*. For example, the price of the option for the bought currency depends on the currency exchange rate, or option for the purchased shares is a financial derivative which value is determined by the value of the shares in question. Institutions emerge as regulators of financial markets are more consent that the financial derivatives dangerously undermine the markets of the original financial instruments that serve as a basis to the financial derivatives.

The most important representatives of financial derivatives are: futures, options, swaps, warrants, convertibles, rights etc. There are views that grouped derivative financial instruments in a different way. For example, financial derivative instruments may be divided into: a) forward - based derivatives, within frames include: futures contracts, forward contracts and swap contracts, b) optional derivatives (option - based derivatives) which include: traditional options (call - put options), swap options (options on swaps) and options for reducing the movement of interest rates and c) exotic derivatives that represents a new forms of financial derivatives with complex features of payment. This type of financial instruments which also develops with the greater development of financial markets, give to investors a variety of forms for protection from financial risk. Exotic derivatives, most often occur in the form of options, including: barrier option - an option that begins to exist, or goes off in specific conditions, binary options - all or nothing options - option in which payments are made only when comes to the occurrence of insured event and multifactor (rainbow) option - an option that is based on various indexes or on a leading securities.

In modern terms, financial derivatives as financial contracts whose payments are based on the execution of a previously agreed activity are part of the economic environment. They can be issued on the basis of money, goods, debt, debt of a company, mortgage housing, shares, interests, and based on a combination of any of stated items or the like. Despite the mentioned categorizations, their general categorization distinguishes (a) optional and (b) forward contracts. Can be listed on stock exchanges or privately traded. Options give buyers the right but not the obligation, at some time to buy or sell certain assets after fixed price, where price is determined (usually small) percentage of the underlying value of assets subject to the option. Forward contracts at its side commits parties (buyer and seller) to trade certain assets at pre-defined fixed price at a future date. Such fixedness determines price risk as for the seller of the assets in question, and for the buyer too, depending on the movement of prices in that interval. Speculations arising from such activities in a form of potential earnings for one side, i.e. for the side with more detailing analytical assessment (i.e. one that will "guess" the market trends) are only one aspect of the use of derivatives. Significant aspect of their use is referencing to the possibility that they are used as an instrument for protection against market risks.

In order to conclude, can be mention. Besides the classical options to insure against the risks facing companies, today are more important place belongs to financial derivatives, by which companies can be insured against adverse movements in market variables. The use of derivatives by financial markets, the firms without mandatory classic insurance in insurance companies can protect themselves from unfavorable changes in foreign exchange, credit risk and business risk.

**Conclusion**

Financial markets are not perfectly competitive, which means that there are asymmetric information on them, so there is a problem in the market signaling. Therefore in practice comes to the process of convergence of the specific areas of the financial industry – and that is the way to relative asymmetric information and they have microeconomic nature, i.e. caused by costs, revenues and profits of the entities on the financial markets.

Liberalization of financial innovation on financial markets in recent decades causes strong growth, causing great quality accommodation. The traditional separation of banking and insurance industry is increasingly narrowing. In fact, banks and insurance companies (and all other financial institutions) adopted a new approach in the business known as bank-insurance in order to achieve an integral approach to financial markets.

Global changes occurring in the financial systems of countries and in the conduct of financial flows in general, introduced major changes in the forms and functions that perform as banking, and non-banking financial institutions. The basic tendency of change is aimed at accelerating convergence of all institutions offering financial services and acceptance of innovations from each other. This tendency is often accompanied by changing the legal framework in the sphere of finance and opening the possibility of different financial institutions to offer financial services that previously were not inherent to them. Such changes create conditions for increasing the number of strong competitors in the financial system are closing banks from all sides and lead to a reduction in their relative participation in the system, in favor of increasing the participation of non-banking financial institutions. The tendency of reducing the participation of banking institutions through their approach to non-banking institutions or vice versa is realized in a way that today's banks and their competitors offer a wide range of similar financial services, the daily enriched with new ones. Such *universalization* of financial services, entities that offer them, and ways that are offered (through the Internet, smart cards, etc.) significantly facilitate the daily activities of their customers. Overall it provides an opportunity at once and on a one place to realize all the financial activities, which in turn leads to the so-called universal banking (in the USA and Great Britain), allfinanz (in Germany) or bancassurance (in France). In that sense can be differentiate more contemporary trends in a banking and non-banking financial sphere and in the financial system in general, that reflect their universality and convergence. In this sense, particularly stand out as worth to emphasize globalization and internationalization of financial institutions; regulation, deregulation and re-regulation of institutions in the financial system; the role of the state on financial markets in the contemporary global environment; reducing the role of financial intermediaries, i.e. disintermediation; changes in the organization and functioning of financial institutions imposing by the technological revolution; the emergence of numerous financial innovations for differentiation of financial products; phenomenon of securitization as a substantial financial innovation; financial engineering and the like.

This is about risk management of financial corporations, insurance companies or banks during they are trading with financial products: the management process by the management structure, with microeconomic objectives - influence of risk on the profits of the insurance or banking corporation.

The problem of complexity of the financial market where the convergence of business trying to ignore the risk by combining financial products on a microeconomic level is resolved through financial derivatives.

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