

DEPOSIT INSURANCE SYSTEM AS A GUARANTEE OF DEPOSITOR'S PROTECTION



O. Yu. SOVA, PhD in economics, Assistant Professor,
National University of Life and Environmental Sciences
of Ukraine

ORCID: 0000-0001-6386-6432

E-mail: sovy@ukr.net



N. POLIAKOVA, student,
National University of Life and Environmental Sciences
of Ukraine

E-mail: poliakova1972@ukr.net

Abstract. The article examines the state and trends in the development of the deposit guarantee system for individuals in Ukraine. The challenges and needs of improving the mechanism of centralized insurance protection of depositors are identified. The authors emphasize the growing role of the Deposit Guarantee Fund of individuals in the banking market and expanding the scope of its modern mechanisms to reduce the negative effects of bank bankruptcy, which is an important factor in ensuring the stability of the banking system.

Emphasis is placed on considering the disposable income of domestic households, as this indicator is an eloquent indicator of improving the country's economic well-being. Parallels were made in the analysis of quantitative indicators of state social guarantees, namely: the expression of the living wage and the amount of the minimum wage for 2016-2020.

The size of the household savings growing is estimated. The importance of converting household savings into investments for economic development is determined and the number of deposits and the value of deposits for households in 2016-2020 are analyzed. The authors also illustrate the dynamics of changes in the UIRD indicator.

The deposit guarantee system is presented as an important factor in the financial stability of the state economy. The article emphasizes the successful steps of legislative regulation of the subject composition of the Deposit Guarantee Fund of Ukraine and reformation of compensation limits, which brings the domestic insurance field closer to European standards of depositor's protection.

According to the results of attracting deposits from the top-9 commercial banks of Ukraine, tables have been formed, the data in which allow making conclusions about the leaders of the deposit services market and the amount of potential reimbursement. Proposals have been formulated to improve the deposit guarantee system, aimed at optimizing insurance schemes and relations in accordance with the threats to financial security as an objective phenomenon of a market economy and the conditions of globalization.

Keywords: bank; banking system; household; income; deposit; saving; interest rates; UIRD; Individual Deposit Guarantee Fund; deposit insurance system; Deposit Guarantee Schemes

Introduction.

The system of individuals' bank deposits protection exists in many countries around the world and it is an important element of risk management of the banking. The deposit insurance mechanism is designed not only to secure depositors' funds, but also to facilitate work with troubled banks, which will prevent crises. Guaranteeing deposits of individuals can be considered as a component of financial security of the country, because it complements prudential banking supervision, enhances the effectiveness of monetary policy, able to stabilize the macroeconomic environment of the state.

Analysis of recent researches and publications.

Many articles are devoted to the study of the functioning of an effective system of centralized insurance of deposits, for example, motives for individuals deposit insurance and deposit insurance system governance were considered (Adema et al., 2019), evolving of initial deposit insurance institutions of post-Soviet countries was analyzed (Horsch et al., 2018). Some papers take a look into the applicable provisions of EU law on the contribution of Deposit Guarantee Schemes in resolution financing (Gortsos, 2019), another one identifies the institutional weaknesses of DGSs and studies their functioning in post-crisis conditions (Kerlin, 2017), there is an analysis of the range of tasks of the deposit insurance schemes (Koziriska, 2020). We consider the next author's opinion as

significant that the strategy of depositing the formation of bank resources should be aimed at adapting the instruments of deposit policy to the changing environment of the banking services market, ensuring the multivariate conditions of placing bank deposits (Sova, 2018). The evolution of international research and practices on building effective deposit guarantee systems in Europe and globally are considered in their best practice recommendations and new regulations (Danylenko, 2017).

But the problems of the functioning of the state deposit guarantee system remain relevant and require further development of promising areas of development, especially in times of economic crisis, such as the protracted coronavirus pandemic.

Purpose. The purpose of the article is to identify trends in reforming the deposit guarantee system of individuals in Ukraine with an analysis of the dynamics of household incomes and deposit interest rates that have developed in the Ukrainian banking system in 2016-2020.

Materials and methods of research.

The study is based on the provisions of the banking legislation of the European Union on deposit guarantee, in particular the Directives 2014/49/EU and 2014/59/EU, Ukrainian legislation, namely, the Law of Ukraine «On the System of Guaranteeing Natural Person Deposits», the Law of Ukraine «On Banks and Banking».

The authors used such general scientific methods of cognition as: generalization – to determine the essence

of household income and **cost** of deposits, comparison – to illustrate the size of state social standards, grouping and analysis of dynamics series – to demonstrate trends in economic indicators, graphical and tabular methods for presenting statistics on selected items during the study period.

Results of the research and their discussion.

From the beginning of 2020, the banking system operates in conditions of unstable macroeconomic conditions caused by quarantine restrictions of COVID-19. Unlike previous financial crises, the situation in Ukraine this time is not accompanied by a reduction in deposits. On the contrary, despite the reduction of interest rates, household deposits are growing. This is encouraging in terms of the rapid intensification of consumer demand after the epidemic situation improves.

Economic growth is impossible without an adequate increase in income. The expansion of disposable household income is the highest factor of economic growing, but at the same time the most difficult in terms of achievement. To ensure it requires a long-term increase in wages, reducing the tax burden on the population. State social programs do not fully achieve such results: it is necessary to qualitatively improve the functioning of market institutions inside the country.

The pandemic has exacerbated the financial inequality of the population, as it has led to falling earnings in low-profitability employment (tourism, hotel and restaurant business, air transport) and increased savings in lucrative industries (digital technology sector, medical goods production).

The income of the population (nominal income) includes cash and material

goods (wages, income and mixed income, property income, social benefits, transfers). The implementation of most of the social guarantees provided for the people of Ukraine depends on the norms of the laws of our state on the state budget, which are adopted annually. For example, in economic terms, the living wage shows how much money a person needs to earn in order to support themselves and not be below the poverty line.

The size of the living wage and the minimum wage in Ukraine during 2016-2020 grew annually, but not at the same rate (Fig. 1).

The minimum wage in 2016 was UAH 1 600, and the living wage was 96,5% of this value. In 2017, the minimum wage was doubled, and the living wage increased by only 10% compared to 2016, and amounted to 53% of the minimum wage. The growth rate of the minimum wage in 2018 was 1,16, and the living wage was 1,1 compared to 2017. At the end of 2020, the minimum wage was UAH 5 000 (20% more than in 2019), and the living wage was UAH 2 270, which is 12% more than in 2019.

It is possible to estimate the size of household savings on the basis of data from sample surveys of living conditions of households in Ukraine, conducted by the State Statistics Service of Ukraine. Let's form a table with data on household income in Ukraine for 2016-2020 (Table 1).

The income of the population of Ukraine amounted to about 2 UAH trln. in 2016 and over the next 4 years we see a growth trend. The growth rate of the indicator was 1,3 in 2017, 1,6 in 2018, 1,8 in 2019, and 1,9 in 2020 compared to 2016. In 2020, the income of the population of Ukraine amounted to almost 4 UAH trln., Which is 7% more than in 2019. The growth rate in 2019 compared to 2018 was 14%.

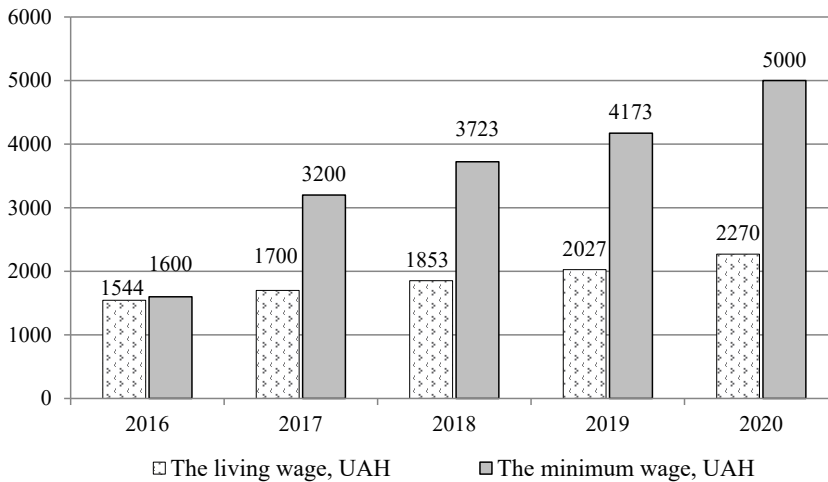


Fig. 1. Ukraine's basic state social standards, at the end of the period, UAH

Source: folded by (Debet-Kredyt, 2021)

Disposable income is nominal income less taxes and other obligatory payments, ie funds used by the population for consumption and savings. The disposable income of the population of Ukraine in 2016 amounted to 1,6 UAH trln., and increased in 2020 to 3 UAH trln., which is 8% more than in 2019. The growth rate of disposable income in 2019 compared to 2018 was 15%.

However, to understand the processes taking place in different consumer markets, it is important not only the indicators of total income (and expenditures), but also the structure of the distribution of these incomes.

Household savings should classically account for a larger share of national savings. If there is no growth, then the resource for the future balanced economic reproduction is not formed. The balance of «savings – investments» makes it possible to reconcile changes in national savings with changes in the financial position of the economy with the outside world.

Changes in the savings of Ukrainians show a negative downward trend: from +12,6 UAH bln. in 2016 to -17 UAH bln. in 2020. The most successful year in the study period was 2018, when the change in saving was +31,5 UAH bln., and 2019 was marked by the outflow of household capi-

Table 1. Household income of Ukraine in 2016-2020

No	Indicator	2016	2017	2018	2019	2020
1	Household income, UAH mln.	2 051 331	2 652 082	3 248 730	3 699 346	3 972 428
2	Disposable income, UAH mln.	1 582 293	2 008 278	2 470 325	2 838 056	3 062 229
3	Change in saving (Increase/Decrease), UAH mln.	+12 591	+30 638	+31 547	-116 165	-17 017
4	Official Exchange Rate UAH versus USD, as of the end of the period	27,19	28,07	27,69	23,69	28,27

Source: folded by (State Statistics Service of Ukraine, 2021)

Table 2. Bank deposit services for individuals in Ukraine in 2016-2020

No	Indicator	2016	2017	2018	2019	2020
1	Deposits by households (outstanding amounts at the end of the period), UAH mln.	444 676	495 313	530 249	576 125	730 317
2	Cost of term person's deposits, %	national currency	16,9	13,8	14,5	14,1
		foreign currency	6,7	3,2	3,2	2,3
3	Interest rates on term person's deposits, %	national currency	17,0	13,8	14,9	14,9
		foreign currency	5,9	3,3	3,3	2,6
4	Integral rate, average weighted, % annual	11,1	8,4	9,7	9,9	5,7
5	Ukrainian Index of Retail Deposit rates (UIRD), national currency, % annual, at the end of the year	17,5	14,3	15,7	15,1	8,7

Source: folded by (National Bank of Ukraine, 2021)

tal with an indicator of -116 UAH bln.. In dollar terms, the change in savings in 2016 was +436 \$ mln., and -602 \$ mln. in 2020.

Determining the importance of converting household savings into investments for economic development, let's analyze the cost of deposits for households in Ukraine (Table 2).

Support of social-political stability is of great importance to ensure a high specific weight of population's savings in banks (Serpeninova, 2014). Bank deposits in Ukraine are in demand among the population, as the risk of investing in other assets is quite high and is not offset by their profitability.

Cost of deposits is understood the total amount of remuneration (a real fee for a deposit) specified in a deposit agreement, including a fee for the use of funds attracted in the form of an interest rate as well as any other costs.

Deposits of households in Ukraine during 2016-2020 increased by 64% from 444,7 UAH bln. to 730,3 UAH bln. (Table 2). The dynamics is constant, and the growth rate is as follows -7,1% in 2018 compared to 2017, 8,7% in 2019 compared to 2018. National Bank of Ukraine publishes the cost of term person's deposits. The indicator in the national currency decreased almost 2 times

in 2020 compared to 2016: from 16,9% to 8,7%. In foreign currency, the indicator decreased almost 5 times: from 6,7% in 2016 to 1,4% in 2020. The most significant reduction in interest rates occurred in 2020.

Interest rates on term deposits obtained by banks from individuals also shows a downward trend. Indicators in 2020 coincide with the values of the cost of term person's deposits of that year in both national and foreign currencies (Fig. 2).

The average weighted integral rate decreased 2 times in 2020 compared to 2016: from 11,1% to 5,7%. In 2018 and 2019, the indicator tended to increase: by 1,3 percentage points in 2018 compared to 2017, and by 0,2 percentage points in 2019 compared to 2018. But the integral rate in 2020 compared to 2019 decreased by 1,2 percentage points.

UIRD (Ukrainian Index of Retail Deposit Rates) – the Ukrainian index of interest rates on retail deposits – an indicative rate calculated each banking day in the Thomson Reuters system based on nominal rates on time deposits of individuals in UAH for a period of 12 months with interest paid after the expiration of the deposit agreement valid in 20 the largest Ukrainian banks by the size of the deposit portfolio of individuals.

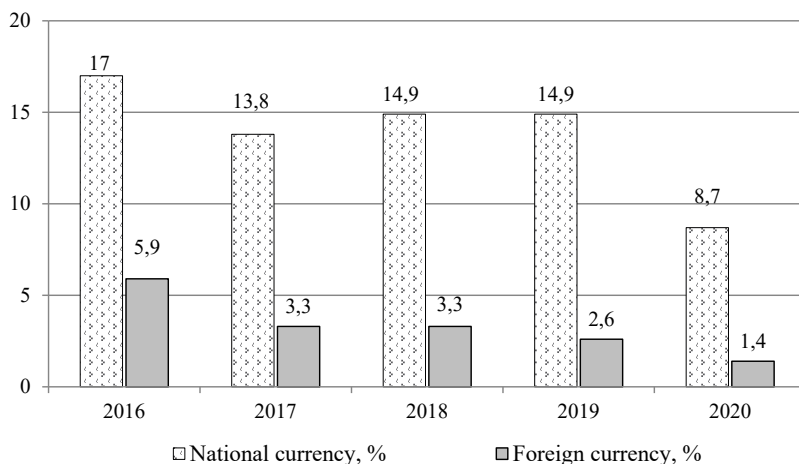


Fig. 2. Interest rates on term deposits obtained by banks from individuals

Source: folded by (National Bank of Ukraine, 2021)

This rate in the national currency also shows a declining trend during the study period: from 17,5% in 2016 to 8,7% in 2020. Last year was not the best for the economy, but favorable for the formation of the resource base of banks and its reduction in price. With a significant amount of liquidity in 2020, banks had the opportunity to save on interest expenses. If at the beginning of the year the UIRD index on 12-month deposits in hryvnia was 15,18% per annum, in dollars – 2,54%, and in euros – 1,09%, then at the end of 2020 – 8,7%, 1,21% and 0,56%, respectively.

The introduction of quarantine measures through COVID-19 has increased the volume and amount of online transactions and strengthened the role of technology. Since October 2020, the National Bank of Ukraine has allowed banks to open accounts remotely using an electronic passport, so the convenience, accessibility and speed of money management came first.

Interest in bank deposit insurance schemes and the discussions on how they function are revived in times of crisis in financial markets (Czechowska, 2018).

It is generally accepted that Deposit Guarantee Schemes play a fundamental role in the financial safety net in three ways (Mecatt, 2020):

- 1) they prevent bank runs by assuring depositors they will have immediate access to their insured funds even if their bank fails (deposit pay-out);
- 2) they avoid banks' disorderly liquidation through a variety of measures (capital support, guarantees, etc.);
- 3) they preserve depositors' access to covered deposits in the context of insolvency proceedings finance, by means of transfer of assets and liabilities and deposit book transfer.

In Ukraine, the Deposit Guarantee Fund of individuals (DGF, 2021) protects the interests of depositors. The Fund's guarantees apply to deposits of individuals in national or foreign currency, including individual entrepreneurs, in all operating banks, except for the Joint-Stock Company «State Savings Bank of Ukraine».

The Fund reimburses each depositor in the amount of the deposit, including interest accrued at the end of the day preceding the day of the Fund's withdraw-

al from the market, but not more than the amount of the maximum amount of reimbursement. From 21.08.2012, the maximum amount of reimbursement on deposits is UAH 200 000, regardless of the number of accounts in one bank.

The Fund's administration is actively working on the implementation of EU Directives, which will allow introducing an early response system and further preventing bank insolvency (Directives, 2014). The aim is to achieve a European level of deposit guarantee – 100 € thous.. Draft Law No 5542-1 of 28.05.2021 passed in the first reading, is a significant step which guarantees the amount of compensation for deposits is planned in the amount of 400 UAH thous., and from January 1, 2023 – 600 UAH thous. (Draft Law, 2021).

Data on deposits of individuals in DGF member increased 1.6 times from 2016 to 2020 (Table 3).

DGF financial resources was 15,7 UAH bln. in 2020. The growth rate compared to 2019 was 50%. But in 2019 compared to 2018 the amount decreased, namely by 28% to the level of 10,4 UAH bln.. The maximum growth rate of DGF financial resources is observed in 2017 by 1,9 times to 14,6 UAH bln..

In order to invest safely, liquidly and profitably, the DGS has to invest in highly rated governmental securities that have a high liquidity, along with the diversification of investments by investment instruments, issues, securities issuers, securities duration and their currency, selecting the most profitable instruments (Žilinskas et al., 2015). Deposit-taking by riskier banks is not restrained by higher contributions to the Fund. We identify two patterns among the variety of approaches to risk-based premiums: formula-based risk-weighting (used in the EU) and scoring-based risk-weighting (used in the US, Canada, Kazakhstan, Malaysia, Taiwan) (Danylenko, 2017).

At the end of 2020, 72 DGF member banks had 607,6 UAH bln. on their household deposit accounts. Thus, JSC «State Savings Bank of Ukraine» has 122,7 UAH bln. deposits.

According to Article 44 of the Law of Ukraine «On the System of Guaranteeing Natural Person Deposits» From the date of liquidation of the bank within three years (in case of liquidation of a systemically important bank – within five years) the Fund ensures the implementation of measures to manage the bank's assets and satisfy creditors' claims (Law of Ukraine, 2021). This explains the figures in rows 3-6 in Table 4, when the number of insolvent banks minus the number of liquidated banks of the previous year does not coincide with the number of banks that the Fund withdraws from the market in the current year.

The number of commercial banks in Ukraine is constantly decreasing: from 96 in 2016 to 73 at the end of 2020. Members of the Deposit Guarantee Fund of Ukraine are all operating banks except JSC «State Savings Bank of Ukraine». The number of insolvent banks under liquidation has halved in 2020 compared to 2017 – from 92 to 46. The process of withdrawal of banks from the market continues, and during 2020, 16 commercial banks have already been liquidated. The year with the largest number of liquidated banks was 2019 – 30 units.

In the spring of 2021, the Cabinet of Ministers supported the draft law «On Amendments to Certain Laws of Ukraine Concerning the Acquisition of JSC «State Savings Bank of Ukraine» the Status of a Member of the Deposit Guarantee Fund for Individuals». For «Oschadbank», joining DGF means an increase in costs due to mandatory contributions – this is 1% of the regulatory capital plus a quarter of the amount of deposits must be paid quarterly.

Table 3. Activity of the Deposit Guarantee Fund of Ukraine in 2016-2020, at the end of the year

No	Indicator	2016	2017	2018	2019	2020
1	DGF financial resources, UAH mln.	7 690,8	14 606,6	14 628,4	10 432,6	15 691,6
2	Number of banks, units	96	82	77	75	73
3	DGF member banks, units (banks during the provisional administration)	99 (4)	83 (2)	77 (1)	74	72
4	Insolvent banks under liquidation, units	81	92	90	58	46
5	Insolvent banks during the provisional administration, units	4	2	1	3	2
6	Banks liquidated, units	18	-	4	30	16
7	Paid out to depositors, UAH mln.	80 865,5	87 924,4	88 906,8	89 740,8	90 131,4
8	Data on deposits of individuals in DGF member banks, UAH mln.	382 150,5	413 769,3	438 353,8	474 440,2	607 564,0

Source: folded by (Deposit Guarantee Fund, 2021)

Paid out to depositors has a constant tendency to increase during the analyzed period. The amount for 5 years increased by 11,5% from 80,9 UAH bln. in 2016 to 90,1 UAH bln. in 2020 (Table 3).

We must not forget about the domestic mechanism of auctions for the sale of assets of liquidated banks, the system «ProZorro.Sale», the first of which took place in November 2016.

A few factors complicate an increased efficiency in the sale of assets of liquidated banks: internal factors (the Fund's lack of resources, including staff, given the scale of the crisis) and external factors, including the slow recovery of economic activity in the aftermath of the crisis and the poor legal protection for creditors (Danylenko, 2017).

Guaranteed compensation payments to depositors are made through the Automated Payment System, which was launched in February 2017. The introduction of the system allows depositors of liquidated banks to apply to any branch of agent banks. At the beginning of 2021, 11 commercial banks were connected to the system.

Let's consider the indicators of banks with the largest number of depositors in Ukraine (Table 4). The data are

entered in the table in descending order of the number of depositors for 2020.

The leader in terms of both the number of individual depositors and the amount of deposits is JSC «PRIVATBANK». In 2019 and 2020, the gap in amounts from the bank on the second step is significant. The number of depositors in 2020 was 22,6 mln. persons, and the amount of deposits 252,7 UAH bln.. The growth rate of the amount of deposits for 2019-2020 was 28%.

The second place in 2019 and 2020 was taken by various banks. In 2020 it was JSC «UNIVERSAL BANK» with the number of individual depositors 3,2 mln., and in 2019 – it was JSC «ALPHA BANK» with the number of individual depositors 2,2 mln.. During the year «UNIVERSAL BANK» increased client portfolio of 1,4 mln. persons. As for the amount of deposits in 2019-2020 the second was «ALPHA BANK»: the amount of 36,2 UAH bln. in 2019 and 43,8 UAH bln. in 2020. Due to the growth in the number of depositors «UNIVERSAL BANK» significantly increased its deposit portfolio from 10,7 UAH bln. in 2019 to 23,2 UAH bln. in 2020.

In 2019 potential reimbursement covered 89,8% of depositors and 80,7%

Table 4. Banks with the largest number of depositors in Ukraine, at the end of the year

No	Name of the bank	Number of depositors, thous. pers.		Amount of deposits, UAH mln.		Potential reimbursement amount			
		2019	2020	2019	2020	thous. persons		UAH mln.	
						2019	2020	2019	2020
1	PRIVATBANK	22 466	22 555	196 790	252 743	17 000	18 070	143 799	179 544
2	UNIVERSAL BANK	1 800	3 192	10 677	23 202	751	1 562	7 699	16 025
3	RAIFFEISEN BANK AVAL	1 974	2 459	29 925	39 153	1 617	1 892	18 022	21 726
4	ALPHA BANK	2 215	2 439	36 159	43 801	811	813	17 128	18 638
5	PUMB	2 032	2 418	21 460	28 536	713	820	11 281	13 932
6	UKRGASBANK	2 085	2 299	25 008	30 237	596	595	13 022	13 964
7	UKRSIBBANK	2 181	2 254	22 690	31 885	1 364	1 382	13 123	16 315
8	ACCENT BANK	1 535	1 766	4 595	6 488	489	526	4 072	5 309
9	OTP BANK	1 025	1 191	16 121	21 884	429	452	6 531	7 687
Total in banks		37 314	40 574	363 425	477 928	23 771	26 111	234 677	293 146
% of total in the Fund		86,0	87,0	76,6	78,7	89,8	91,0	80,7	82,9
TOTAL in the Fund		43 379	46 621	474 440	607 564	26 471	28 687	290 872	353 539

Source: folded by (Deposit Guarantee Fund, 2021)

of deposit amounts. In 2020 – 91% of depositors and almost 83% of deposit amounts. Banking system has a good perspective to continue to attract capital and generate sufficient profits.

Conclusions and future perspectives of the study.

Thus, deposit insurance is a widely used and integral part of the financial safety provided by states including Ukraine.

Interest in bank deposit insurance schemes is recovered in times of crisis on financial markets. Therefore, it is necessary to timely and effectively reorganize and improve the domestic deposit insurance system so that it can meet all the challenges of a cyclical economy.

Promising ways to improve deposit guarantee systems in Ukraine are:

- 1) cooperation of deposit insurance and bank resolution authority to strengthen the relationships between the participants of financial safety system;
- 2) increasing the efficiency of sales of insolvent banks' assets for growing the sum of the available financial resources of the DGF to perform its functions;
- 3) improving the approaches to calculation of risk-based premiums to achieve a macroprudential effect – higher price of deposit resources for market institution in case of high risk of operations;
- 4) enhancement the operational readiness for the payment of guarantee compensation to depositors and the calculation of the amount of depositors' claims;
- 5) strengthening financial discipline in the insurance market through the use of a joint insurance mechanism;
- 6) extending coverage to retail deposits at other credit institutions to provide

the protection of depositors of financial institutions that are not members of the DGF;

- 7) identification the measures to mitigate moral hazards when growing the covered amount because system protects the parties against losses, which weakens market discipline among banks and depositors;
- 8) overcoming low financial literacy of households on deposit guarantee issues to prevents weak social groups from becoming impoverished.

The deposit guarantee system must be dynamic, ie respond to the challenges facing the financial system. Thus, the Deposit Guarantee Fund of individuals is a necessary institution that provides trust to depositors, increases their confidence in the depository system and has all the prospects for further operation and development.

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Анотація. У статті досліджено стан та тенденції розвитку системи гарантування вкладів фізичних осіб в Україні. Визначено виклики та потреби вдосконалення механізму централізованого страхового захисту вкладників. Авторами підкреслено зростання ролі Фонду гарантування вкладів фізичних осіб на банківському ринку та розширення сфери застосування ним сучасних механізмів зниження негативних наслідків банкрутства банків, що є важливим фактором у забезпеченні стійкості банківської системи.

Зроблено акцент на розгляді наявних доходів вітчизняних домогосподарств, адже цей показник є красномовним індикатором підвищення економічного добробуту країни. Проведено паралелі в аналізі кількісних показників державних соціальних гарантій, а саме: виразу прожиткового мінімуму для працездатних громадян та суми мінімальної заробітної плати за 2016-2020 роки.

Оцінено розмір приросту заощаджень домогосподарств. Визначено важливість перетворення заощаджень населення в інвестиції для розвитку економіки та проаналізовано кількість вкладів та вартість депозитів для домогосподарств у 2016-2020 роках. Також авторами унаочнено динаміку змін показника UIRD.

Систему гарантування вкладів представлено як важливий чинник фінансової стабільності економіки держави. У статті наголошено на успішних кроках законодавчого врегулювання суб'єктного складу Фонду гарантування вкладів України та реформування компенсаційних лімітів, що наближає вітчизняне страхове поле до європейських стандартів захисту вкладників.

За результатами залучення депозитів топ-9 комерційними банками України сформовано таблиці, дані в яких дозволяють зробити висновки про лідерів ринку депозитних послуг та обсяги можливого страхового покриття. Сформульовано пропозиції щодо вдосконалення системи гарантування вкладів, націлені на оптимізацію страхових схем і відносин між учасниками відповідно до загроз фінансовій безпеці як об'єктивного явища ринкової економіки та умов глобалізації.

Ключові слова: банк; банківська система; домогосподарства; доходи; депозити; заощадження; процентні ставки; UIRD; Фонд гарантування вкладів фізичних осіб; система страхування депозитів; схеми гарантування вкладів.