

International Congress on Economics, Management and Business Studies
Hosted Online from New York, USA
Date: 23rd September, 2026
Website: https://econferencia.com

ANALYSIS OF FACTORS THROUGH WHICH THE INSTITUTIONAL DEVELOPMENT OF THE SECURITIES MARKET AFFECTS FINANCIAL STABILITY

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ABSTRACT

This article systematically examines the factors through which the institutional development of the securities market influences financial stability. It analyses the interrelationships among regulatory quality, corporate governance, market depth, secondary-market liquidity, the investor base, and clearing and settlement infrastructure. In the context of Uzbekistan’s capital market, the study assesses risks arising from the concentration of trading activity and interconnectedness with the banking sector. The findings distinguish between positive and adverse transmission channels and propose an indicator-based monitoring framework.

Keywords: securities market, institutional development, financial stability, liquidity, market depth, investors, corporate governance, systemic risk.

Introduction

Within the global financial system, the securities market constitutes an important institutional platform for transforming savings into investment, facilitating price discovery for capital, and allocating financial risks. Its development offers enterprises financing opportunities beyond bank lending, mobilises public- and private-sector resources over longer horizons, and diversifies the structure of financial intermediation. Nevertheless, an increase in the size of the capital market does not, in itself, guarantee financial stability: a high degree of

concentration, short-term speculative capital flows, sudden liquidity shortages, and disruptions along the settlement chain may accelerate the transmission of economic shocks. Institutional development must therefore be assessed not only in terms of trading turnover but also in relation to market resilience and its capacity to absorb risks.

In Uzbekistan, capital market development is closely linked to the transformation of state-owned and state-participated enterprises, privatisation, the expansion of corporate bond issuance, and the diversification of long-term investment funding. At the same time, the dominant role of banks in financing, the low proportion of freely tradable shares in certain market segments, and the limited institutional investor base make it necessary to assess the quality of institutional reforms separately. Accordingly, this study aims to classify the principal factors through which the institutional development of the capital market affects financial stability, explain their transmission mechanisms, and develop a system of indicators suited to the conditions of Uzbekistan.

The study employs institutional, comparative, structural, and systems analysis. The analytical dimensions comprise regulation and transparency, market depth, secondary-market liquidity, investor diversification, clearing and depository infrastructure, and interconnectedness between the banking sector and capital markets. For each factor, a positive transmission channel, a potential adverse externality, and a monitoring indicator are identified. The research is conceptual and analytical in nature: because comprehensive annual and comparable micro-level statistical series are unavailable, no regression coefficients or causal-effect magnitudes are estimated. Accordingly, correlation is not equated with causation. The methodological framework includes the market-capitalisation-to-GDP ratio

(MC/GDP × 100), the turnover ratio (annual secondary-market trading volume divided by average free-float market capitalisation), issuer concentration (HHI = Σs_i^2), cross-exposures to banks, the bid–ask spread, settlement failures, and changes in investor composition. Where market shares are expressed on a scale from 0 to 1, the HHI also ranges from 0 to 1; a higher value indicates greater concentration of trading among a limited number of participants. These indicators should be calculated over consistent periods and for comparable categories of instruments. The proposed set of indicators is not an independent composite index but a methodological framework for subsequent statistical monitoring.

The analysis indicates that the relationship between institutional capital market development and financial stability is not unidirectional. Effective supervision and disclosure reduce information asymmetry, whereas poorly designed incentives or disproportionate requirements can increase the cost of entering the market. A deep and liquid market improves investors' ability to dispose of assets without substantial discounts. However, when investors employing similar strategies initiate simultaneous sales, stronger market interconnectedness may transmit shocks more rapidly. The assessment of institutional development must therefore consider both the stability-enhancing and stability-weakening mechanisms associated with each factor.



Table 1. Transmission Channels Through Which Institutional Factors Affect Financial Stability

Factor	Positive transmission channel	Potential risk	Monitoring indicator
Regulation and transparency	Confidence and price discovery	Disproportionate requirements	Reporting quality; regulatory breaches
Market depth	Access to alternative capital	Dependence on major issuers	Market capitalisation/GDP; free float
Secondary-market liquidity	Rapid, low-cost exits	Sudden evaporation of liquidity	Turnover; spreads; trading days
Investor diversification	More stable demand	Herding and similar portfolio strategies	Investor shares; HHI
Clearing and depository infrastructure	Lower counterparty risk	Operational disruption	Settlement failure rate
Bank–market interconnectedness	Risk sharing	Cross-sector shock transmission	Cross-exposures

The factors presented in Table 1 are closely interconnected. For example, regular disclosure by issuers reduces investors' valuation errors; however, if the free float remains low, transparency alone cannot generate sufficient liquidity. Similarly, a modern trading platform facilitates faster price discovery, but when market participation is narrow, large orders may have a disproportionate effect on prices. Technological modernisation and institutional deepening are therefore not substitutes; rather, they must be coordinated within an integrated policy framework.

Public market reviews have reported that trading turnover on Uzbekistan's stock market in 2024 was approximately UZS 19.6 trillion. Because a substantial share of this volume was attributable to individual large transactions, growth in

aggregate turnover cannot be interpreted as an equivalent increase in everyday secondary-market liquidity. This example supports an important methodological conclusion: one-off block trades, primary placements, and regular secondary-market transactions should be recorded separately. Otherwise, the market's capacity to absorb sales during shocks without substantial price declines may be overestimated.

Table 2. Indicators for Distinguishing Market Activity from Financial Stability

Indicator	What it measures	Implications for stability
Total trading turnover	Value of all transactions	Reflects activity, not liquidity in itself
Turnover excluding block trades	Intensity of regular trading	Closer approximation of secondary-market liquidity
Free float	Share of equities available for public trading	Price discovery and market accessibility
Bid–ask spread	Difference between quoted buy and sell prices	Transaction costs and liquidity stress
HHI	Concentration of issuers or investors	Higher values indicate concentration risk
Settlement failures	Transactions not completed on time	Signal of operational vulnerability

The findings summarised in Table 2 demonstrate why market development should not be evaluated using a single indicator. For example, high turnover may coexist with wide bid–ask spreads, a low free float, and considerable concentration. Under such circumstances, the market remains vulnerable to sharp asset-price declines during external shocks. Stock-exchange statistics should therefore encompass not only the aggregate value of transactions but also daily

trading frequency, average transaction size, the proportion of large trades, and measures of price impact. Policy decisions regarding institutional effectiveness should be informed by the joint dynamics of these indicators. Another important aspect of financial stability is the transmission of risk between the capital market and the banking sector. Banks may operate as securities issuers, investors, underwriters, or intermediaries. Although these activities promote the diversification of funding sources, a decline in the prices of common assets may simultaneously affect bank balance sheets and investor confidence. In particular, when large transactions involving state-participated enterprises and banks increase overall market size, it is essential to examine whether the independent investor base has expanded accordingly. Financial stability oversight therefore requires data exchange and coordination among securities regulators, banking supervisors, and macroprudential authorities.

Table 3. Measures to Strengthen the Contribution of Institutional Development to Financial Stability

Priority area	Implementation mechanism	Expected outcome	Evaluation criterion
Transparency	Standardised issuer reporting	Reduced information asymmetry	Timely submission of reports
Liquidity	Market making and trading statistics	Improved price discovery	Bid–ask spread and trading frequency
Diversification	New issuers and investors	Reduced concentration	HHI; free float
Operational security	Clearing and settlement stress tests	Lower disruption risk	Settlement failure rate
Macroprudential supervision	Mapping bank–market risk exposures	Earlier identification of shock transmission	Cross-exposures

The measures set out in Table 3 should be implemented in a coordinated sequence. The first priority is to improve the underlying statistical database and distinguish market segments accurately. Subsequently, incentives to enhance trading liquidity should be aligned with corporate governance requirements. Before introducing market-making arrangements, the obligations of market participants, continuity of quotations, conflicts of interest, and supervisory requirements must be clearly defined. In depository and clearing infrastructure, emergency preparedness, operational continuity, and cybersecurity should receive particular attention. To assess effectiveness, baseline indicators should be established and recalculated quarterly using a consistent methodology.

A limitation of this study is the lack of publicly available, continuous data series for numerous important market microstructure indicators. Thus, although the classification presented in this article provides a basis for theoretical and policy-oriented conclusions, demonstrating the precise quantitative effects of these factors would require panel data, information on banks' securities exposures, issuer-level free-float data, and transaction-level trading statistics. Future research should prioritise stress-testing the effects of liquidity shocks on bank capital, examining the relationship between trading concentration and price volatility, and comparing the periods preceding and following institutional reforms.

CONCLUSION

The study finds that the effect of securities market institutional development on financial stability is multidimensional and conditional. Regulatory quality, corporate governance, information transparency, secondary-market liquidity, diversity of the investor base, and the reliability of settlement infrastructure are key determinants of market resilience to shocks. Their beneficial effects are

reflected in market confidence and efficient capital allocation, whereas unbalanced development may intensify concentration, price instability, and the transmission of systemic risk. In particular, higher aggregate trading turnover should not be equated with genuine improvements in secondary-market liquidity: large block trades and short-term transactions may increase recorded market activity without sufficiently strengthening continuous price discovery. For the further development of Uzbekistan's capital market, the article recommends standardising issuer reporting, regularly disclosing free-float and trading-concentration measures, fostering competition among brokers and institutional investors, enhancing the operational resilience of settlement infrastructure, and including cross-exposures between banks and securities markets in macroprudential monitoring. Financial stability assessments should jointly consider market capitalisation, trading volume, bid–ask spreads, turnover ratios, the HHI, settlement failures, and investor composition. An integrated monitoring dashboard based on these measures would help evaluate the outcomes of institutional reforms and identify emerging vulnerabilities at an early stage. Future research should test these conceptual conclusions using econometric analysis and stress tests based on comparable statistical series.

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