MODEL FOR AN INSURANCE MARKET ANALYSIS. NEW CHALLENGES FOR COMPANIES MANAGEMENT

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Abstract

In this paper we present some considerations about the Romanian insurance market and its evolution for the last six years. The insurance companies are important players of the financial market, serving a number of economic functions, such as allowing risk transfer; helping companies and people save and invest, enabling entrepreneurial spirit and business initiatives.

All these are possible only on a stable and developed market. In order to describe our internal insurance sector we used some particular indicators such as gross written premium volume, insurance density and insurance penetration rate.

Based on our conclusions we submit some directions to be followed in order to overstep the present situation of our insurance market. We think that some decisions must be taken by insurance companies management because more often lately insures are being reproached for their exclusive concern for rising profits despite of their basic activity and function which is delivering a proper financial cover for the policy holders.

Key words: insurance market, insurance density and penetration, management, diversification strategy, product innovation

JEL Classification: A1, G2, M1

1. Introduction

Previously seen as one of the most dynamic and promising activity field of our economy, the insurance sector is nowadays challenging major evolutions that requires proper interventions from the supervisory authority and insurers management.

Before the global economic recession, the insurance sector grew more than most fields of the Romanian economy. For some years, the rate of development in terms of gross written premium volume exceeded the Romanian GDP.

In spite of this favourable evolution, other major insurance indicators such as insurance density and penetration rate were far below similar indicators from EU countries.

Hereinafter our intention is to describe the present situation and also the Romanian insurance market development for the last six years (2009-2016) using some particular indicators such as gross written premium volume for the entire market and for each major category – life insurance and non-life insurance, insurance density, insurance penetration rate or the amount of paid claims.

2. Literature review

Our paper contains two major parts: one is dedicated to the Romanian insurance market evolution and the other presents some solutions for overstepping the present unfavourable situation of this sector.
Regarding the first part, the main insurance indicators are largely explained in the insurance literature (Văcărel, Bercea, 2003), (Bistriceanu, 2010), their importance for a proper analysis of the market being presented in many papers.

Also the Financial Supervisory Authority provides every year a complete quantitative analysis of the insurance sector.

For the second part, there are a few papers dedicated to management in insurance companies (Constantinescu, 2004, 2000), this domain being less analysed by our specialists.

3. Insurance market analysis

The information provided for 2009-2014 by the Financial Supervisory Authority – which is responsible for regulating and supervising the insurance market – shows us a decline from the level of gross written premium volume reported in each prior year with one exception: there was a real growth of this indicator with 2.15% in 2012 (table 1).

According to FSA, after these years of premium volume decline, the insurance market returned to positive growth in 2015. In 2015 the gross written premiums increased with 8.23% to RON 8.75 bn from the level reported in december 2014.

If we analyse the Romanian insurance market in terms of insurance density (gross written premiums per capita) and insurance penetration (gross written premium in GDP-%) we will find out that Romania has ones of the lowest values of these particular indicators in EU and also their dynamics were negative for the past few years.

### Evolution of gross written premium on Romanian insurance market (2009-2014)

<table>
<thead>
<tr>
<th>Year</th>
<th>Gross Written Premium (RON)</th>
<th>GWP Growth $t_x/t_{x-1}$ (%)</th>
<th>Inflation rate (%)</th>
<th>GWP Real Growth $t_x/t_{x-1}$ (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2009</td>
<td>8,869,746,957</td>
<td>-0.74</td>
<td>5.59</td>
<td>-6.00</td>
</tr>
<tr>
<td>2010</td>
<td>8,305,402,152</td>
<td>-6.36</td>
<td>6.09</td>
<td>-11.74</td>
</tr>
<tr>
<td>2011</td>
<td>7,822,309,952</td>
<td>-5.82</td>
<td>5.79</td>
<td>-10.97</td>
</tr>
<tr>
<td>2012</td>
<td>8,256,914,950</td>
<td>5.56</td>
<td>3.33</td>
<td>2.15</td>
</tr>
<tr>
<td>2013</td>
<td>8,122,446,890</td>
<td>-1.63</td>
<td>3.98</td>
<td>-5.39</td>
</tr>
<tr>
<td>2014</td>
<td>8,085,676,884</td>
<td>-0.45</td>
<td>1.07</td>
<td>-1.51</td>
</tr>
</tbody>
</table>

Source: Financial Supervisory Authority Report 2014 (www.asfromania.ro)

But it is also a fact that insurance density and penetration decreased in EU in 2014 due to the international financial environment but the levels of these indicators for our internal insurance market are far below the EU average rate or similar emergent european markets. Data available (source: www.asfromania.ro) for 2013 indicated that Netherlands and United Kingdom have the highest level of insurance penetration rate (11.7%) while insurance density for Nederlands was around 4,491.4 EUR per capita.

Also for 2013 Hungary has 2.71% the insurance penetration rate and 275.5 EUR per capita the insurance density level, also Poland 3.47% and 257.4 EUR per capita.

1. Financial Supervisory Authority - The Evolution of Romanian Insurance and Reinsurance Market, december 2015
the Bulgarian market reported 2.15% the insurance penetration rate and 121.2 EUR per capita for the insurance density in 2013. For the same period, Romania reported 1.27% for the insurance penetration rate and 92 EUR per capita for the insurance density (table 2).

Insurance density and insurance penetration rate for the Romanian market (2009-2015)

<table>
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</thead>
<tbody>
<tr>
<td>Insurance density (RON per capita)</td>
<td>435.49</td>
<td>410.21</td>
<td>388.25</td>
<td>411.61</td>
<td>406.41</td>
<td>405.35</td>
<td>440.41</td>
</tr>
<tr>
<td>Insurance penetration rate (%)</td>
<td>1.74</td>
<td>1.56</td>
<td>1.38</td>
<td>1.41</td>
<td>1.27</td>
<td>1.21</td>
<td>1.24</td>
</tr>
</tbody>
</table>


The positive dynamics of gross written premiums for 2015 had a favourable influence on insurance density evolution – FSA reported a 0.03 percentage points growth for 2015 from the level reported ([www.1asig.ro](http://www.1asig.ro)) for the same period of 2014 (1.21%).

Also according to the insurance supervisory authority insurance penetration rate experienced a 8.64% growth, thus, reaching the highest level of the last six years – 440.41 RON per capita. The insurance industry trend based on gross written premium volume before, during and after the economic crisis is presented using figure 1.

We can see that the Romanian insurance market is not back yet to its best level from 2008 which is not a strong point for this economic sector. Looking at the insurance market from the geographically risks spreading view we observe that 49.88% of the gross written premiums are delivered in 2014 by the Bucharest-Ilfov area, which is a long distance from the level of 8.95% delivered by the North-West area of the country.

The Romanian global insurance market is dominated by non-life insurance. This line of business gave 79.27% of the gross premiums subscribed at the level of the entire market in 2015, which is, in fact, a slightly decline from 2014 when the level was around 79.75%. Life insurance delivered 20.72% from the gross written premiums in 2015, more than last year when the similar indicator was around 20.25%.

In the same time, the claims paid last year by the Romanian insurance companies for the non-life insurance policies were 95.77% from the claims paid by the entire market in 2015 (which is a growth from 2014 when the percent was about 90.18%) while for the life insurance contracts the market paid only 4.23% (the percent decreased from 9.82% in 2014).

According to the Financial Supervisory Authority, in 2015, 85.76% of the non-life gross written premiums are delivered by three lines of business (69% for 2014):

- Car insurance (class 3) with 24.33% of non-life premiums;
- Fire and natural disaster insurance (class 8) – 13.92%;
- Motor third party liability insurance (class 10) – 47.41%.

These three lines of insurance business are sharing the gross claims paid for the non-life policies. For example, in 2015 the insurance industry paid for the motor third party liability insurance contracts around 53.79% of the entire claims (48.6% in
2014), 33.00% for the car insurance policies (35.81% in 2014) and only 4.85% for the fire and natural disaster insurance line (5.08% in 2014). Therefore the Romanian insurance industry is dominated by the motor insurance – a high loss ratio line of business.

Gross written premium volume for 2006-2015

According to Financial Supervisory Authority, for example, 55.35% of gross written premiums in 2014 represent the gross claims paid for non-life and life insurance contracts. Under these circumstances we wonder if the insurance market is prepared to pay losses produced by a major earthquake?

Another important feature of Romanian insurance sector is that the market is highly concentrated. 79.25% of gross written premiums (both life and non-life) were delivered in 2015 by ten insurance companies. This situation has a negative impact towards market competitiveness and influences the quality of services delivered to the policy holders. Under these circumstances the bankruptcy of Astra – the third largest insurance company in 2014, with a market share of 9.52%, 1.8 million policy holders and 2.5 insurance contracts will seriously affect the entire sector.

Although many insurance specialists consider Astra’s bankruptcy as a „maturity exercise” for our internal insurance market, we think that this event will decrease people’s trust in the market’s capacity to deliver the expected coverage for their needs and also will create a number of difficulties in the process of paying the insured claims.

Of course, according to our legislation for such cases there is the Romanian Insurance Guarantee Fund. Every month the insurance companies pay 1% of the gross premium incomes for non-life insurance contracts and 0.4% of the gross premium incomes for life insurance contracts².


1. FSA Law no. 16/2015 and Law no 17/2015 relating to the Romanian Insurance Guarantee Fund, published in M.Of. no. 667/2015

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Revista Română de Statistică - Supliment nr. 5 / 2016
In 2016 the Romanian justice system issued a definitive decision regarding Astra’s bankruptcy. Under these circumstances, all of Astra’s claims requests will be managed by the Romanian Insurance Guarantee Fund. The clients had to to wait almost one year, giving the fact that Astra’s shareholders went to court to appeal the decision of the Financial Supervisory Authority to suspend its license and send it into bankruptcy.

On the other hand, the Romanian Insurance Guarantee Fund had confronted in the past with another insurers bankruptcies such as ADAS, Croma, GrupAs, Metropol, Euroasig, Delta Addendum, but none of these companies weren’t as large as Astra.

Beyond the fact that the bankruptcy of a large insurance company on a highly concentrated market is not the most wanted event, we should analyse its consequences on short term as well as on the medium and long term, but more important, we must identify all its causes in order to prevent future similar events.

ASTRA has been under special administration for 18 months starting February 2014 after the Financial Supervisory Authority discovered the solvency and liquidity indicators of the insurer were not meeting the legal requirements. KPMG Advisory was named to run the company during the special administration process, with the task of finding a strategic investor that could restore the insurer’s financial strength. After one year and a half, the insurer failed to increase its capital, therefore FSA suspended its licence and began bankruptcy procedures.

The Financial Supervisory Authority discovered the following causes for Astra’s bankruptcy: the defective Astra’s management which had used the insurer’s assets in order to attend to some private interests from Astra Group1 and a distorted reporting of financial performances and solvency and liquidity indicators.

This situation confirms what Douglas G. Olson, an american insurance specialist, frequently quoted in our previous papers, studying the insurance companies, observed: „in history of majority insurance companies’ bankruptcies there are more causes related to incompetent management and fraudulent behaviour than the negative actions of market factors.”

Although the insurance market is highly regulated and supervised it seems that FSA’s instruments were not enough or appropriate.

In 2005 when the insurance companies were forced to significantly increase their capital (with some of them dissapearing after that) we underlined that it musn’t be the size of an insurer the most important criterion to eliminate companies from the market. It is neccesary to analyse the risks undertaken by an insurer, the assets and liabilities management along with solvability and liquidity indicators.

Conclusions

Although the preliminary results for 2015 show a recovery of insurance premiums, the market problems still exist and they are getting bigger. We think that the solutions for market recovery and growth must be found at three levels: at the FSA level, the insurance companies management level and the policy holders level.

First of all, the Financial Supervisory Authority must play its active task as a regulation, supervisory and control authority on the insurance market, in the absence or keeping the distance from different scandals which may affect its credibility and

1. Source: Financial Supervisory Authority Press release
reduce people’s trust in its capacity to protect policy holders interests. We think that the new personnel recruiting policy and public relation strategy along with some decisions related to the market are better and appropriate for a more efficient supervisory authority.

About FSA’s instruments, we consider that implementing Solvency II in 2016 will increase the efficiency of the supervisory activity, giving the fact that this new legal requirements are based on risks analysis.

Second, as far as the orientation towards clients remains only a market slogan and it isn’t undertaken by all decision levels in an insurance company, the situation isn’t going to change soon.

In a competitive environment which allows only a slow development, the insurance companies’ capacity to deliver the promised value to the policy holders depends firstly by the rational understanding of organizational strengths and the insurers’ ability to adjust their activities according to the external movements.

Nowadays, to achieve a balance between profitability and social responsibility of insurance companies is a major challenge for them. More often lately insures are being reproached their exclusive concern for rising profits, despite of their basic activity and function which is delivering a proper financial cover for the policy holders.

In order to rise insurers’ competitiveness and to carry on a performant management in this domain, we have defied a series of managerial approaches such as: strategic management, management based processes orientation, management methodologisation or changing organizational culture.

We think that for the next period companies should establish clear strategic options in order to deliver a proper competitive advantage. Among these are: diversification of insurance portfolio, increasing efficiency of their activities, involvement in peoples education towards insurance for a better understanding of its necessity and importance.

The Romanian insurance market is dominated by motor insurance products characterised by a high loss ratio. Therefore, in order to improve the underwriting results, it is necessary to promote other insurance products, such as: homeowners insurance, agriculture insurance and professional liability insurance.

Besides these, the insurance supply should adapt to the financial possibilities of the clients and deliver simple and affordable mass-market solutions. Product innovation is a rational choice for insurance companies doing business on an emergent market. Insurers must design products that offer more comprehensive life protection, help mobilise savings and enable wealth accumulation, especially for low-income population.

Also another major management aproach should be the improvement of risks management procedures and reinsurance covers.

It is very important for the insurance companies to fulfill their major function: to provide clients a proper coverage at a competitive price and to pay insured losses in order to raise people’s trust in the insurance market capacity to protect them against all kind of risks.

The third aspect is that clients should know that they are dealing with risks and the best protection against them is an insurance policy. We know that the price of an insurance contract is very important in choosing the right company and the
most suitable insurance product but it shouldn’t be the only criterion. Usually a low
premium rate could be a good deal for the policy holder but this price cannot guarantee
the future payments of the insurers, especially for the high ratio lines of insurance
business.

The insurance market represents a major component of the financial market.
Its main function is to compensate the losses caused by natural disasters and accidents
and to pay sums insured for some life events. Besides that major function the insurance
sector is an important part of the economy, significantly influencing the amplitude and
duration of economic cycles, the social and economic progress. This activity sector
also contributes to the economic development and quality life improving. All these
are possible only if the insurance companies remain competitive, pay claims and do
business under transparent conditions and circumstances.

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