UDC: 338.2 (4-11+4-191.2)
Original Scientific Paper
Accepted February, 22, 2018
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ANALYSIS OF THE BUSINESS OF THE INSURANCE SECTOR IN THE COUNTRIES OF CENTRAL AND EASTERN EUROPE IN THE CONDITIONS OF THE CRISIS

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Abstract: *This paper presents the key indicators of the insurance sector business in the countries of Central and Eastern Europe in the conditions of the global economic crisis, in the period 2007-2012. The authors of this paper work on the assumption that the insurance sector affects the development of the economic and financial system of selected countries in the region of central and eastern Europe (eight countries were analyzed: Serbia, Croatia, Montenegro, Bosnia and Herzegovina, Macedonia, Romania, Bulgaria and Albania). With the start of the crisis, the analyzed countries managed to maintain stable growth (or stagnation) of premiums. A higher growth rate was recorded in the life insurance segment. However, unlike developed markets, non-life insurance dominated the portfolio structure, about fifteen times the penetration rate was recorded, as a result of the low level of GDP per capita. According to the criterion of the insurance density, the insurance market in the analyzed countries is lagging behind the developed financial systems, recording several tens of times lower insurance density. Bearing in mind the mentioned facts, we can conclude that the analyzed countries have significant potential for the development of the insurance sector in the future.*

Keywords: *insurance sector, economic development, Central and Eastern European countries, global economic crisis*

1. INTRODUCTION

Theoretical and empirical research has shown that countries with a more developed financial system achieve faster and more stable growth and development. The financial system in the analyzed countries of central and eastern Europe has several common features:

- Insufficiently developed, unstable and risky to invest in comparison with the countries of the European Union.
- "Bankocentric" financial system, or system in which there is a dominant share of the balance sheet and capital of the banking sector.
- Inadequate portfolio of the insurance sector with the dominance of non-life insurance and insufficiently developed life insurance segment.
- Insufficient initiative for the development of new financial products, primarily in the life insurance segment, which can significantly accelerate the development of the entire financial system.

Financial institutions that are the most important players in the financial system differ in their functions, roles and features. However, what is common to all financial institutions is the role of intermediaries which they perform by collecting financial resources through their own free cash that they further direct to deficit entities. Financial intermediaries can be divided into four groups [Vasiljević, 2006]:

- traditional or classical intermediaries (banks, savings banks, etc.);
- collective investors (investment companies, mutual funds);
- broker-dealer institutions (stock brokers) and
- institutional investors (insurance companies, pension funds, financial companies, endowments, etc.).

Apart from the banks, insurance companies are the most important financial institutions that play a key role in the development of the economy. The task of insurance is to manage risks in the most efficient manner and to ensure a stable development of the national economy (in the first place, establishing social stability), thus stimulating responsible behavior of business entities in relation to their property and citizens, not only in terms of property, but also in terms of their health and securing a peaceful age [Kočović, 2008]. Insurance is a mechanism for collecting financial resources on the market. Like other financial institutions insurance companies also mobilize financial surpluses, citizens' savings, which are then directed to deficit entities. In this way, they represent intermediate financial institutions, since with the sale of life insurance policies the insurance company mobilizes savings, and in the event of the death of the insured person, they pay compensation to family members, which is a form of contracted savings on the one hand and insurance from the financial loss of the family in case of premature death [Krstić, 1997].

Insurance companies in the financial market seek to find unique methods and strategies of business that will achieve a sustainable competitive advantage. In other words, in order to ensure long-term survival in the market, they tailor their offer to the needs and demands of consumers (insurance service users). Insurance belongs to a group of service activities in which the insured pays the insurance premium, and the insurer in return takes the risk, satisfies the needs of the consumer and "ties" him to the company. Like financial intermediaries, insurance companies also accept premiums to use as the remaining funds after payment of their costs and calculating reasonable profit [Krstić, 1997].

2. INSURANCE SECTOR IN CENTRAL AND EASTERN EUROPEAN COUNTRIES

Insurance companies, just like institutional investors, are important players in the financial market, primarily in the capital market. The significance of the activities of insurance companies is reflected in ensuring financial stability and strengthening competition in the financial system. In the future, insurance companies can easily take over the position of leading financial investors as they are part of a group of institutional investors with large amounts of capital (which are no longer measured in millions, but in billions of dollars). Observing the dynamics of global insurance development over the past ten years, the growth of the share of insurance in the global financial system has been noticed in relation to other financial institutions.

In the early 1990s, in developed European countries, significant transformations of banks and insurance companies occurred, which were reflected in the disappearance of strict differences between these activities. Namely, in order to maximize profit and improve overall performance, financial institutions took over the activities of other intermediaries. Today, most banks provide insurance services, while a significant number of insurance companies are moving towards the offer of banking products and services

Two decades ago in the analyzed countries of Central and Eastern Europe, the process of economic and social transformations was initiated with the aim of creating a modern market economy. In such conditions for the insurance market, it can be said that it has the potential for development, primarily for the improvement of life insurance. The role and significance of the insurance sector and its growth in the financial system can best be seen by a comparative analysis of the banking sector and the insurance sector in the selected countries of Central and Eastern Europe.

The undertaken reforms in the region, in the insurance sector, enabled the creation of a reliable and stable market that provides security and quality to security users. However, it is evident that the insurance sector, according to the criterion of assets and realized capital, is far behind the banking sector in the group of countries analyzed. In addition, the insurance sector in the region lacks a greater supply of new products (primarily in the life insurance segment), which can accelerate the development and accelerate the growth of this segment of the financial system. New products and business models from the world of modern insurance to countries in the region usually come with smaller or (much more often) bigger delay, mostly due to:

- conservative approach of the management of insurance companies;
- providing exclusively traditional insurance products;
- insufficiently developed citizens' awareness of the role and significance of the insurance sector;
- economic and political instability in the region.

In order to determine the level of development of the insurance market in the region, this section will show a comparative analysis of the insurance sector in the period 2007-

2012. years based on the following development criteria*: realized insurance premium and portfolio structure of insurance companies and degree of development of insurance market (penetration and insurance density).*

3. LEVEL OF REALIZED INSURANCE PREMIUMS AND PORTFOLIO STRUCTURE

In the period 2007-2012 earnings from insurance premiums in the European Union reached the level of 1.093 billion euros [Insurance Europe, 2014]. The total insurance premium in the world in 2011 decreased by 0.9% in real terms, with the decline in developed countries at 1.2%, while developing countries achieved modest real growth in total insurance premium of 1.1% and Central and Eastern European countries 3.9% [NBS, 2012]. However, the total premium in the analyzed region recorded a decline of 15.1% in 2012 compared to 2007. In 2011, Britain had the largest share in the total premium at the European Union level, with approximately 20%, followed by France, Germany and Italy, accounting for 44.3% of the European Union's premiums. On the other hand, the lowest participation in the insurance premium in 2011 was held by Iceland, Malta, Estonia and Lithuania [Insurance Europe, 2014].

Numerical values of insurance premiums and insurance structure in selected countries in the region in the period from 2007 to 2012. Countries in the region are well below the EU average premium, which confirms that the aggregate insurance premium ranged from 7.3 billion euros (as recorded in 2012) to 9.3 billion euros (as achieved in 2008). In the period 2007-2012 the years of the highest insurance premiums were recorded on the Romanian and Croatian insurance market with a share of approximately 60% in the total premium of the analyzed countries. On the other hand, the countries with the lowest degree of development of the insurance market are Albania and Montenegro with an insurance premium of 49 to 67 million euros (Central Bank of Albania and Montenegro).

Compared to 2007, in 2012 five of the eight countries analyzed increased the level of insurance premiums, with Montenegro and Albania dominating in this group (growth rate above 30%). With the onset of the crisis in 2008, all countries managed to maintain a steady growth of premiums, ranging from 4.2% in Serbia to as much as 21% in Romania. Additionally, 50% of analyzed countries recorded a higher increase in insurance premium than the region average (14.9%). However, in 2009, due to the negative effects of the economic crisis, a decrease in insurance premiums was observed in all analyzed countries. At the level of the region there was a fall of 21.4 p.p. compared to 2008, the most drastic reduction was recorded in Romania (47 pp). In 2010, the analyzed countries recorded a real growth of total insurance premium of 2.7% with the rise in life premiums and a fall in the non-life insurance premium. The increase in life insurance premiums was the result, first of all, of savings products of shorter maturity, while the sales risk of life insurance products remains low. The non-life insurance market of this region is particularly affected by the slow recovery of the economic situation in most countries in the region and low investment activities [NBS, 2011].

One of the most important indicators of the degree of insurance development is the insurance structure. The insurance structure shows the level of participation of non-life and life insurance premiums in the total insurance portfolio. In the context of the insurance structure, it should be noted that life insurance in the countries of the European Union is dominant in relation to non-life [Dimić, 2015]. Considering the fact that in countries with a developed insurance market, the share of life insurance in the total insurance premium is increasing from year to year (for example, the insurance market in Liechtenstein, Great Britain and Finland), it is not surprising that in the countries of the European Union precisely this type of insurance has a primacy over non-life insurance. In the portfolio of insurance companies in 2011, life insurance accounted for 59%, while non-life insurance accounted for the remaining 41% [Insurance Europe, 2013].

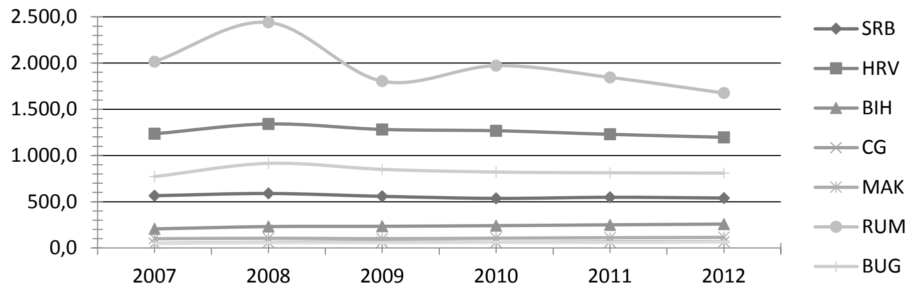

Fig. 1. *Insurance premiums in countries of central and eastern Europe (in millions of euros)*

Source: Websites of Central Banks of Central and Eastern European Countries

Unlike the countries of the European Union, in the analyzed countries in the region, the situation is diametrically opposite. In this context, we have already mentioned that the biggest problem in the group of analyzed countries in the region is the insufficient development of the life insurance segment. For example, the lowest level of participation of life insurance premiums was recorded in Macedonia (2.8% in 2007) and then in Albania. When it comes to Serbia, we have to bear in mind that the share of life insurance [Hanić & Kočović, 2006] in 2001 was less than 1% and that in the previous years a significant step was made in creating positive preconditions for a more dynamic development of life insurance, and the level of life insurance in the insurance structure in 2012 was at the level of 19.3%. The largest share of life insurance in the countries in the region was recorded in Croatia (around 27%) and Romania (about 20%) [Central Bank of Croatia, Central Bank of Romania].

4. PENETRATION AND DENSITY OF INSURANCE

The insurance sector in countries in the region is still underdeveloped and, according to the development, is well below the average of the countries of the European Union.This is confirmed by, certain indicators of the development of the insurance market. The most important indicators of the development of the insurance market are penetration ratio and density ratio of insurance. While penetration of insurance measures the share of insurance premium in gross domestic product (GDP), the insurance density represents the insurance premium per capita and is at the same time an indicator of a payable demand.

As a result of the fall in premium levels in Europe and the negative effects of the global economic crisis, the average penetration of the insurance market in the European Union fell from 7.7% in 2008 to 7.7% in 2011 [Insurance Europe, 2013]. Figure 2 shows the market penetration index which in the period 2007-2012 did not exceed the level of 2.9% in the countries in the region. The highest share of premiums recorded in GDP was recorded in Croatia, Bulgaria and Montenegro (over 2%), while the weakest developed insurance market was in Albania with penetration rate around 0.6%. Compared with the analyzed countries in the region, the domicile insurance market is not in enviable position, ahead of Albania, Macedonia and Romania, at about the same level as the insurance market in Bosnia and Herzegovina. Analyzing statistical data, we found that in 2012, according to the criterion, the penetration rate in Serbia was the worst ranked in the 61st place (only Romania was worse at 69th place), while Croatia and Bulgaria ranked 40th and 56th respectively [Sigma, 2012].

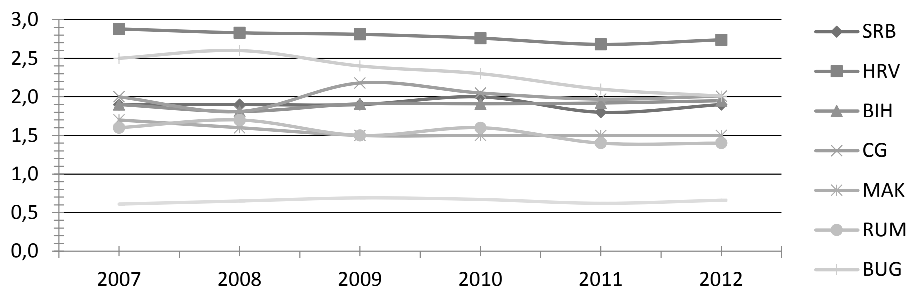

Fig. 2. *Penetration of insurance in Central and Eastern European countries*

Source: Websites of Central Banks of Central and Eastern European Countries

Compared with the penetration rate of countries in the European Union, we can conclude that the insurance market in the region in the group of countries analyzed is below the average of EU member states. In addition, penetration of insurance in the countries of the European Union in the period 2007-2011 ranging from 7.7% to 8.7%, which is even 14 times more compared to the results achieved in the group of countries surveyed in the region [Insurance Europe, 2013]. The low penetration value in Serbia is due to the low level of GDP per capita. Namely, there is a direct correlation between the insurance premium and the gross domestic product: with the increase in the gross domestic product per capita, the insurance premium increases(much faster than the gross domestic product), and vice versa, with the decrease in the gross domestic product per capita, insurance premium decreases.

According to the criterion of the insurance density, the insurance market in analyzed countries in the region lags behind the EU member states, recording up to 90 times lower insurance premiums per capita. The average security density in the European Union in the period 2007-2012 ranged from EUR 1,813 to EUR 2,041 [Insurance Europe, 2013]. The difference in the degree of development of the insurance market in the analyzed countries of the region is more noticeable when comparing the Albanian insurance market, which is at the same time at the lowest level of development, with the countries of the European Union. Under the conditions of the crisis, in 2009, the most pronounced decrease in the insurance density is in the group of analyzed countries. Thus, in the observed year, in six of the eight analyzed countries, a trend of decreasing insurance premiums per capita was present (the most drastic decline at a rate of 25.7% was recorded in Romania), while Montenegro and Bosnia and Herzegovina managed to keep the growth trend (chart number 3). By comparative analysis of countries in the region, we can conclude that the insurance density in Croatia is almost 14 times higher than in the market in Albania. Thus, in 2011, the lowest security of 21 euros was recorded in Albania, while Croatia was the leader in the region with a premium per capita of around 280 euros. It is encouraging that in 2012, five of the eight countries analyzed managed to increase the insurance security ratios, while on the other hand, Romania, Serbia and Bulgaria retained the downward trend in the insurance premium per capita.

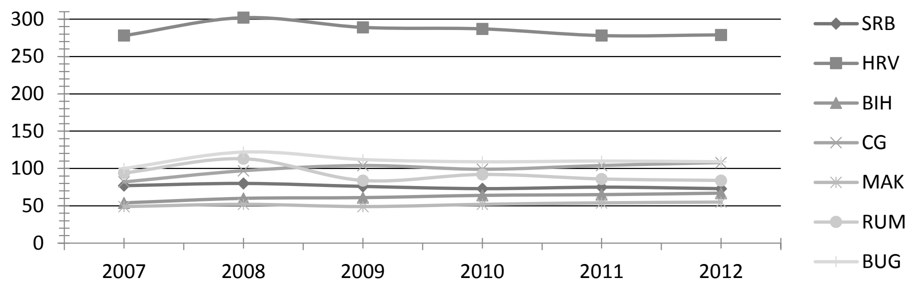

Fig. 3 *Density of insurance in the countries of central and eastern Europe, in euros*

Source: Websites of Central Banks of Central and Eastern European Countries

Compared with the analyzed countries in the region, the domestic insurance market is five-tier, it is in the table in front of Albania, Macedonia and Bosnia and Herzegovina. According to the premium per capita of 73 euros, Serbia ranks 69th, with the same indicator for countries in the region at 218 euros [Sigma, 2013]. High insurance density and increased awareness of insurance coverage mean less potential for premium growth in the coming years. Bearing in mind this fact, we can conclude that the countries analyzed in the region of Central and Eastern Europe, recording several tens of times the lower insurance density compared to the developed countries in Europe, have great potential for the development of insurance in the future.

5. CONCLUSION

All parameters of insurance development (total insurance premium, penetration and insurance density) indicate that the analyzed region lags behind developed countries. Regarding the total insurance premium, countries in the region are below the average of the total insurance premiums earned in the European Union. However, it is encouraging to note that in comparison with 2007, five of the eight countries analyzed increased the level of insurance premiums in 2012, while 50% of the analyzed countries recorded a higher increase in insurance premium than the region average (15%).

Historically, in the structure of portfolios in the analyzed countries, the non-life insurance segment has the dominant share. The life insurance market in countries in the region is still underdeveloped in relation to the countries of the European Union in which this form of insurance dominates and approximately accounts for 2/3 of the realized insurance premiums. The real growth in total insurance premiums was accompanied by an increase in life premiums and a fall in the premium of non-life insurance. The increase in life insurance premium was the result of savings products of shorter maturity, while the sales risk of life insurance products is still low. The non-life insurance market is particularly affected by the slow economic recovery of most countries in the region, as well as the low level of investment activities. The difficult economic and social situation has led to the fact that the number of life insurance policies is not at a satisfactory level, that is, that the total life insurance premium has a low share in the total insurance premium in the countries in the region. In this context, in order to make the insurance market in the region modern and efficient, it should change the existing insurance structure and achieve a more dynamic growth of life premiums compared to non-life insurance. The insurance market in analyzed countries in the region has great potential for development, but there are numerous challenges that are related to the current financial and economic situation in the region. We can expect that analyzed countries in the region, having recorded several tenths of times lower share of premiums per capita, as well as the share of premiums in GDP, in relation to the countries of the European Union, will achieve faster growth in comparison with markets with higher penetration and security density.

The insurance sector in the analyzed countries of the region remained stable in times of crisis. No major oscillations were recorded in the level of total insurance premium, market penetration and insurance density. The development of insurance (primarily life insurance segment), through the mobilization of free funds, can significantly contribute to the progress of the financial system and the economy. Sustainable economic growth stimulates the development of the financial sector, which contributes back to a more successful and even more dynamic economic advancement.

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