

ANALYSIS AND CURRENT TRENDS OF THE INSURANCE MARKET IN LATVIA

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ABSTRACT

This paper considers and analyses current trends of the global, European and Latvian insurance markets. Insurance constitutes the most important way to minimize and eliminate economic losses in a company resulting from unfavourable events. Insurance is one of the most efficient methods of enterprise risk management. The entrepreneur must be informed regarding the offered insurance services, the insurance market participants and the insurance market state for the insurance coverage implementation. This information will enable to provide reliable insurance coverage in order to ensure the enterprise's financial stability. The authors analyse the financial activity index and conduct its comparative analysis, establish general trends and existing differences in the insurance market development in the world, the EU and in Latvia. The paper highlights the insurance market structure and differences in the scope of the life insurance sector existing in the EU and in Latvia. Moreover, description of insurance types, participants of the insurance market in Latvia and the insurance market's state are also provided. The findings can be used by insurers and entrepreneurs for insurance coverage implementation in Latvia.

KEYWORDS: *insurer; life insurance, non-life insurance, real premium growth.*

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Introduction

The need for own protection in case of adverse events generates the need for insurance, and the opportunity of loss covering initiates insurance interest of the person straining after insurance coverage. The need for insurance service, which can be provided by an insurance company with its interest in form of income from insurance activity, arises in such a way. Insurance business efficiency in terms of these interests' protection is obvious and proved in the process of contemporary socio-economic relations development. Insurance constitutes a reliable protection mechanism and provides the owners with social and economic stability by means of damage reparation in case of the property damage or loss, and also in case of income loss by entrepreneurs and the population due to unforeseen events affecting their property interests. Insurance provides continuity of all socially beneficial activity types and people income after certain events, e.g., insured events. Currently, the choice of an insurance company is no less important than the designated bank or investment

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fund choice. Insurers should provide the insurance market with modern insurance products for implementation of effective insurance logistics for the consumer, in particular, for the enterprises executing international cargo carriage.

Insurance companies must regularly monitor trends and dynamics of the insurance market both at the global and European level, and in the insurance implementation country, i.e. in Latvia, in order to determine the priorities in the market conduct, in the long-term and in the nearest prospects. The insurance market is evaluated by the scope and expansion factors of real insurance premiums, i.e.: by the funds that insurance companies obtain from the policies sale in general and by product types; insurance penetration and the concentration factor. However, there are practically no such studies of the insurance market in Latvia.

The findings of research may be used by insurers and entrepreneurs in planning the insurance coverage and ensuring business risk management of Latvian companies. The authors suggest using the findings for the subsequent study of the insurance market, namely, transport insurance sector, and for development of carriage enterprise logistics insurance.

The aim of research is to determine the compliance of insurance protection with the current EU requirements and the possibility of implementing the risk management program in enterprises in Latvia on the basis of the insurance market analysis in the world and in Europe in the long- and short-term perspective.

The tasks of research:

- To identify and characterize general trends in the volume of collected insurance premiums (real premium growth) at the global insurance market in the long-term perspective;
- To analyse financial index seeking to evaluate the European insurance market status (as of the beginning of 2018) with the forecast for the short-term perspective;
- To establish the insurance market development trends based on the volume of collected insurance premiums (real premium growth) and non-life insurance related services in Latvia.

The object of research is the non-life insurance service.

The subject of research is implementation of the risk management program in enterprises in Latvia with the help of insurance.

The theoretical and methodological basis of the study is works of foreign and local authors analysing insurance issues, namely: K. Brandmeir, M. Grimm, A. Holzhausen, S. Crawford, L. Russignan, K. Kumar, A. Huertas, M. Lerner, N. Novozhilova.

In accordance with the intended aim and objectives of the study, we defined the research methods at the theoretical and empirical level. The general scientific principles of development of economic knowledge were used as the methodological basis, namely, classification, generalization, and analogy. Also, the following techniques and methods were employed: statistical analysis (correlation, comparison, extrapolation); method of positive and normative analysis and synthesis, which allowed examining the phenomena and processes in development, identifying the contradictions, and correlating the essential characteristics and forms of their manifestation. The methods of indices and expert assessments, the method of financial ratios and elements of risk theory were also used in solving specific problems. The software package STATISTICA (SPSS) and MS Excel spreadsheets were used as a tool in solving practical problems.

The information base of research was the current regulatory framework of the EU and Latvia on insurance and reinsurance, official data of the European insurance and reinsurance federation, Financial and Capital Market Commission of the Republic of Latvia, Latvian Insurers Association, studies of Organisation for Economic Co-operation and Development, Allianz, Research Munich, Deloitte annual and quarterly newsletters, materials from Swiss Re Sigma.

1. General trends at the global insurance market in the long-term prospects

After the period of financial and economic crisis which occurred in 2008, the world economy demonstrated the financial index growth in 2017 (Economic Research Data Allianz Group, 2018). Similar trends are

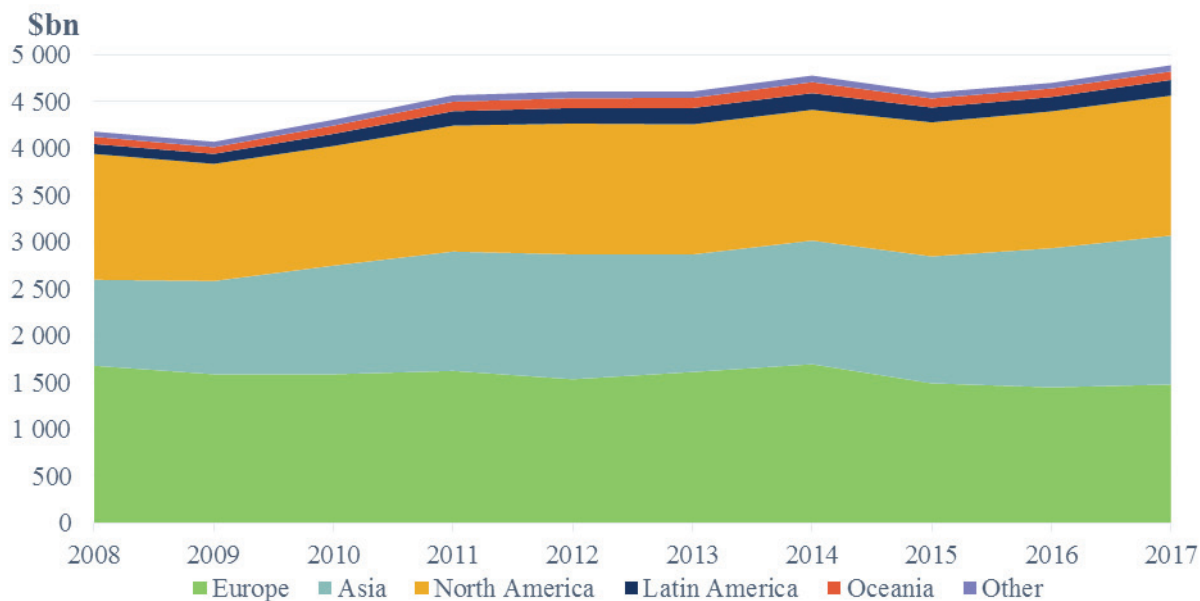


Fig. 1. World insurance premiums in 2008-2017 (\$bn)

Source: Insurance Europe 2018.

observed in the insurance sector. In 2017, the global insurance market grew up to almost 5 trillion US dollars level in terms of the written premiums (Figure 1).

The premium growth rate, according to Allianz Research data (Allianz Group Research, 2018), slightly increased in 2017 compared to 2016 (+2.9%) and it lagged behind the economy growth rate (nominal growth makes +5.9%), which is observed for the second year in a row. Thus, the insurance penetration (rise of premiums' percentage against GDP) has decreased to the level of 5.5%, the lowest mark over the last 30 years (Brandmeir, Grimm, Holzhausen, 2017). Yet analysts consider this situation paradoxical as this figure was on average one percentage point higher at the beginning of the 21st century, before the great financial crisis (Crawford, Russignan, Kumar, 2018).

Following the researchers from the Allianz group forecasts, in the next decade, the insurance market will continue to grow at a rate up to 5.9% per annum, but not evenly across the world regions (Economic Research Data Allianz Group, 2018; Brandmeir, Grimm, Holzhausen, 2017).

In North America, we expect the market growth to double from 1.9 percent to 3.7 percent (Brandmeir, Grimm, Holzhausen, 2017).

On the other hand, in many emerging markets, we predict slightly slower growth, albeit still at a much higher level than in the developed world (Brandmeir, Grimm, Holzhausen, 2017). Markets of the countries with the developing economy, especially in China, are characterized as having greater potential for rapid growth, at least in percentage terms, especially for the companies dealing with property insurance (Lerner, 2017; Insurance Europe Annual Report, 2018).

A report by Swiss Re's "Sigma" research unit (Swiss Re Sigma, 2018) found that emerging market of P&C premiums increased 9.6% in 2016, compared to the overall global growth of 3.7% in China, the world's third-largest insurance market, with non-life premiums increase of 20%. At the moment, the insurance premiums not related to life insurance have increased by 20% in China, which constitutes the third largest insurance market in the world (Swiss Re Sigma, 2018).

The Chinese life insurance market has grown by 21% in 2017, having significantly exceeded the average ten-year index making 14% (Brandmeir, Grimm, Holzhausen, 2017). China has become the second largest

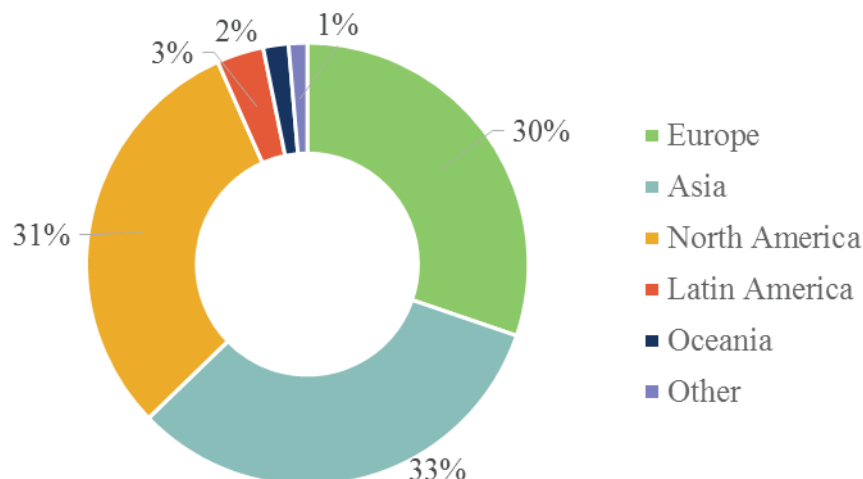


Fig. 2. Distribution of insurance premiums in the world in 2017 (%)

Source: European Insurance — Key Facts (2018); Swiss Re Institute (2018).

life insurance market after the USA and accounts for more than half of the insurance premiums in the emerging markets insurance sector, or 11% of the total global amount (Lerner, 2017).

The Latin American region and a large number of Asian emerging markets, for example, are likely to continue reporting double-digit growth rates over the next ten years, with the Chinese insurance market leading the pack. This means that one in three euros of additional premiums will be earned in China during this period (Deloitte, 2018; Brandmeir, Grimm, Holzhausen, 2017).

Express growth is expected in Western Europe countries: after zero growth in the period between 2008 and 2016 (Huertas, 2018), premiums are expected to grow to the level of 3% per year by 2027 (European Insurance – Key Facts, 2018).

According to Swiss report, following the results of 2017 (Swiss Re Institute, 2017), the European insurance market accounted for 30% of the written premiums sector (Figure 2).

European non-life premiums account for 28% of 2017 global non-life premiums (European Insurance – Key Facts, 2018).

Summarising, the Eastern European insurance markets reported relatively robust growth averaging 5.8% a year between 2008 and 2016. Despite this, only 1.5% of global premium income, or an estimated EUR 54 billion or so, was written in this region last year, an amount that corresponds to only one-third of the German insurance market (Allianz Group Research, 2018; European Insurance – Key Facts, 2018; OECD, 2018). Half of this amount, in turn, was attributable to the two biggest markets, Russia and Poland, alone (Brandmeir, Grimm, Holzhausen, 2017).

Insurance penetration (gross written premiums as a percentage of GDP, in % of GDP) in developing economy countries is growing faster than in countries with developed economy. Insurance penetration in Europe in 2017, in relation to 2016, increased by 0.14 of a percentage point to 7.53% and ranged from 0.9% in Latvia to 12.2% in the UK (European Insurance Outlook, 2017). This confirms the positive development trends at the insurance market.

Therefore, it can be stated that it is observed the general trend of positive growth of written premiums, i.e., the demand for insurance products and insurance market expansion.

2. Development trends observed in the insurance product sector at the world market

The total of European written direct gross premiums in 2017 amounted to EUR 1,213 bln., of which the share of EUR 710 bln., or 59%, accounts for life insurance (European Insurance – Key Facts, 2018), which is conventional for developed insurance markets (Lerner, 2017). The following insurance types account for significant shares in the branch: life, health, motor, property, general liability, casualty. The total share of the most demanded types of insurance accounts for 95% of the insurance market. The structure of the written premiums’ insurance market in Europe is presented by types in Figure 3 (constructed according to European Insurance – Key Facts, 2018).

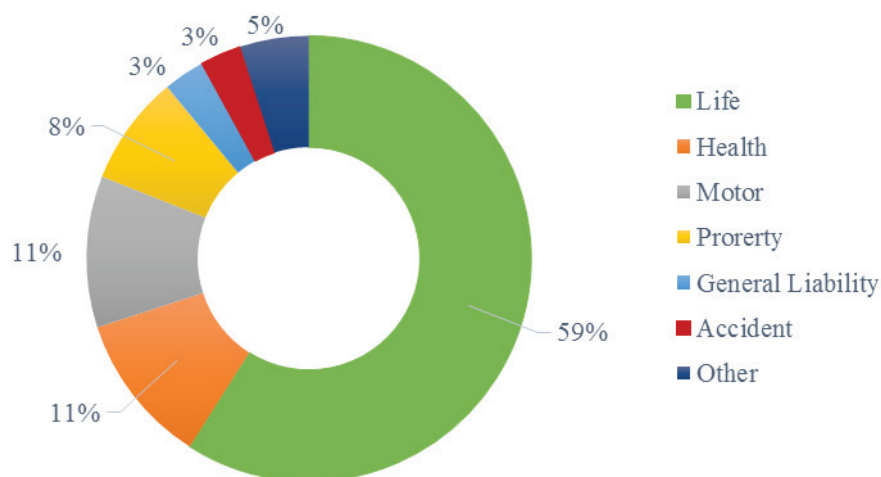


Fig. 3. Structure of the written premiums’ insurance market in Europe

Source: constructed according European Insurance — Key Facts (2018).

As a result of data analysis, it can be stated that the life insurance market share makes over 50% (Crawford, Russignan, Kumar, 2018), both in the world and in other countries with developed economy: Japan, UK, France, South Korea, Italy, Taiwan (Figure 4).

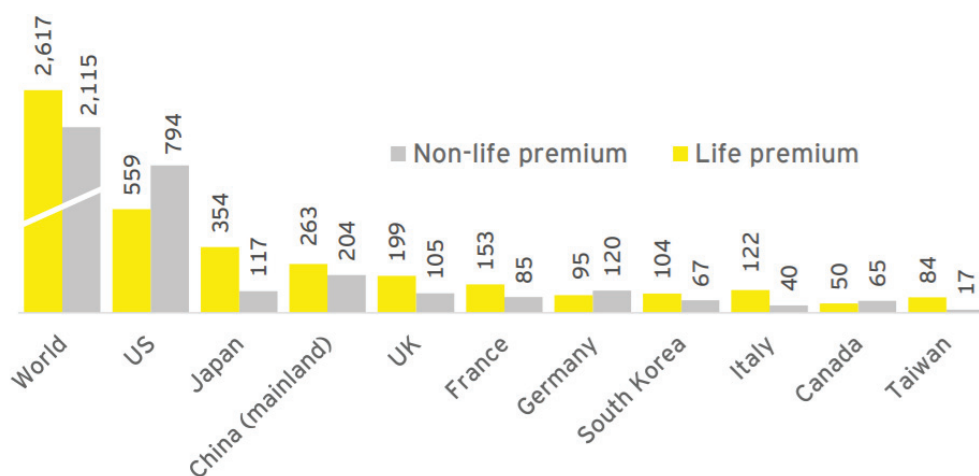


Fig. 4. Global gross written life and non-life insurance premiums in 2016 (US\$b)

Source: Global insurance trends analysis (2018: 28).

This insurance type (life insurance) prevails over the share of all other types taken together and, of course, each type taken separately (Figure 3). Shares of health and motor transport insurance that are the most demanded insurance types second to the share of life insurance market are equal and make only 11%. This insurance type is top requested, since life insurance policies are treated as securities in these countries and fully operate in the financial market. It should be noted that this status of life insurance policies is absent in Latvia, which stipulates the much lower demand (see Section 3).

As a result of analysis, it was revealed that life insurance in Europe is generally more developed than non-life insurance in such countries as the USA, Germany and Canada. At the same time, pursuant to the Global insurance's evaluation (Crawford, Russignan, Kumar, 2018), life insurance premiums decreased in 2017, since the majority of basic markets have reduced or remained at the same level mainly due to insurance product reduced attractiveness under low interest rate conditions – the life insurance sector in developed markets failed to recover from the financial crisis that occurred in 2008. This trend is negative and to date the change prospects based on the available data is a challenge. Life insurance low yield remained a problem in most markets due to the considerable share of existing life insurance liabilities with integrated guarantees (European Insurance Outlook, 2017). And statistical information regarding non-life insurance in Europe in 2017 confirms the marginal growth trend and stable profitability (Insurance Europe, 2018). The data analysis enabled to reveal that the current trend of the written premiums volume growth is a result of significant premiums growth in such countries as Great Britain, Germany, France and Spain (Moody's Investors Service, 2017).

Short-term prospects. The analysis confirms the prospects of stable development of the life insurance market in the period of 2018–2019. Trends in the advanced markets steady growth, in parallel with the growth of the emerging market share enable to predict that the global life insurance market will increase by 4% by 2019 (Figure 5).

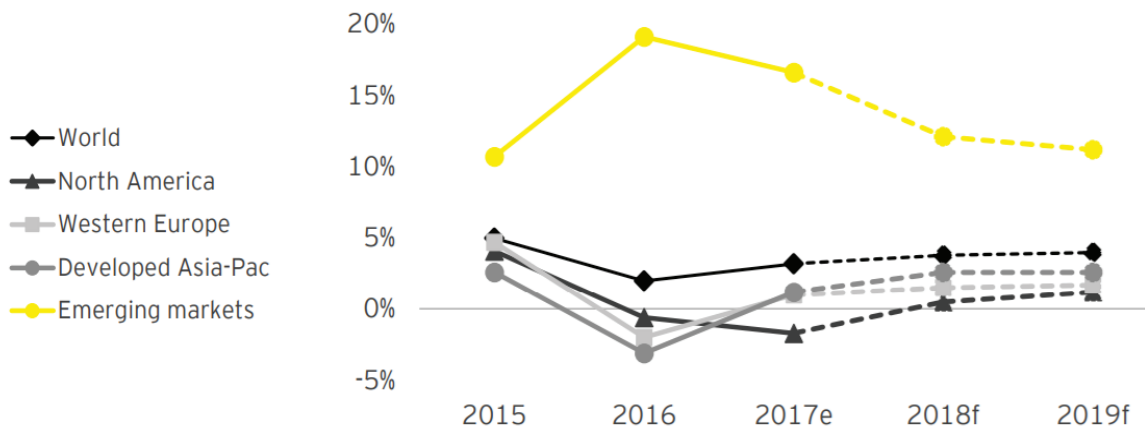


Fig. 5. Global life insurance GWP growth (2015–2019)

Source: S. Crawford, L. Russignan, K. Kumar (2018: 9).

The prospects of non-life insurance in the period of 2018–2019 (Figure 6): the demand for non-life insurance is expected to start in the period of 2018–2019 as the global economic scenario gradually improves with emerging markets continuing to be the main driver (Crawford, Russignan, Kumar, 2018).

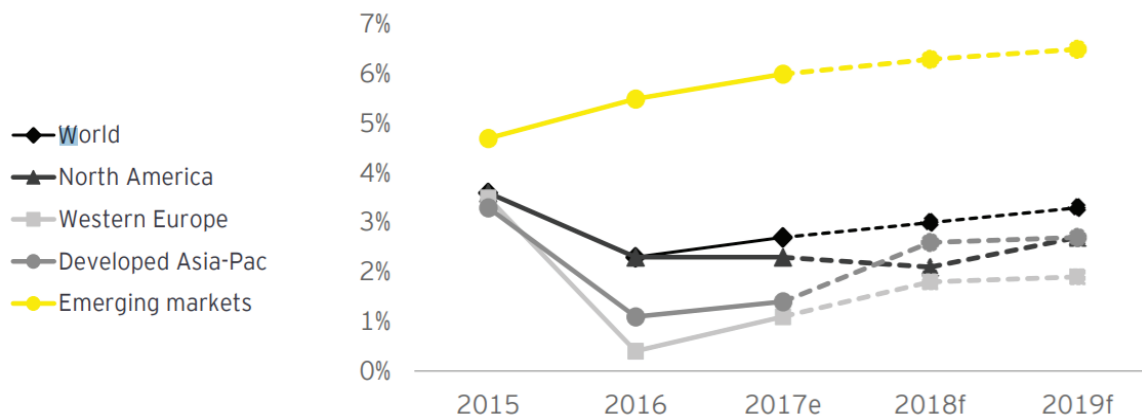


Fig. 6. Global non-life insurance GWP growth (2015–2019)

Source: S. Crawford, L. Russignan, K. Kumar (2018: 10).

The findings reveal that the volume of the written premiums related to P&C (property and casualty) and health insurance makes 50% and more of the insurance market in sixteen countries of Europe out of 28. The distribution is presented in Figure 7, data for Latvia are provided as well.

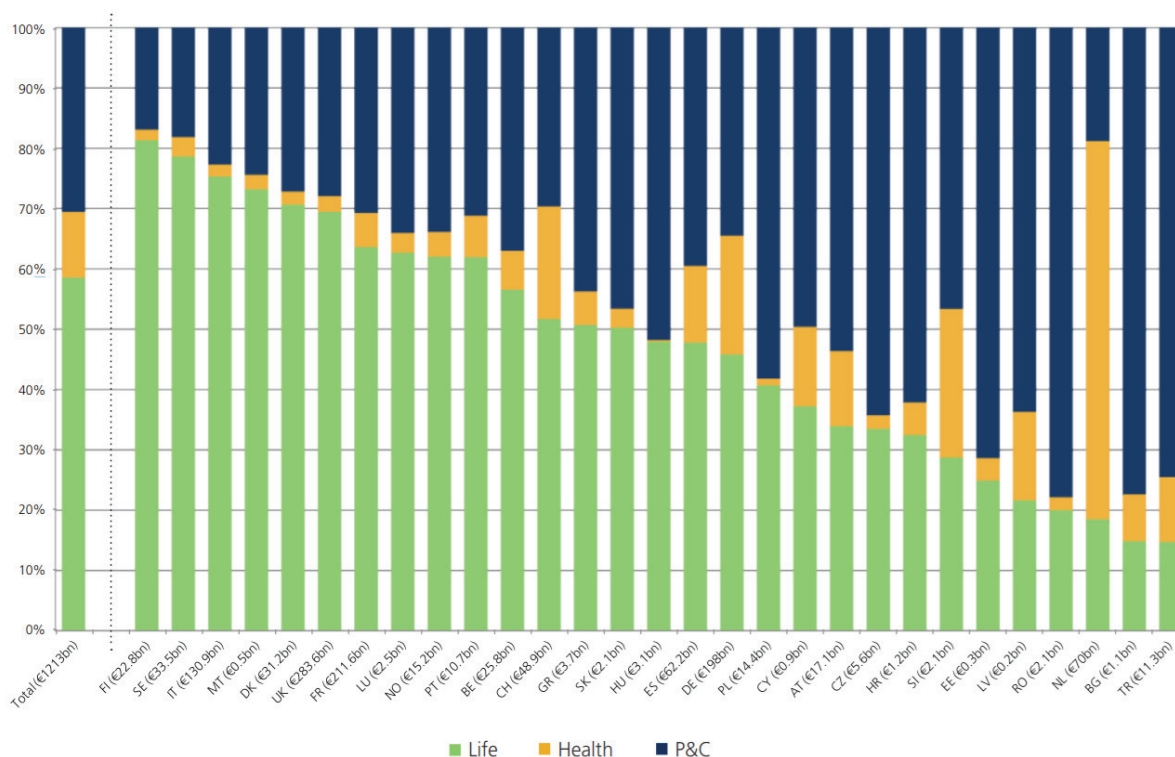


Fig. 7. Gross written premiums by country in 2017

Source: European Insurance – Key Facts (2018: 12).

The volume of the written premiums related to P&C (property and casualty) insurance makes 50% and more of the insurance market in eleven countries of Europe out of 28.

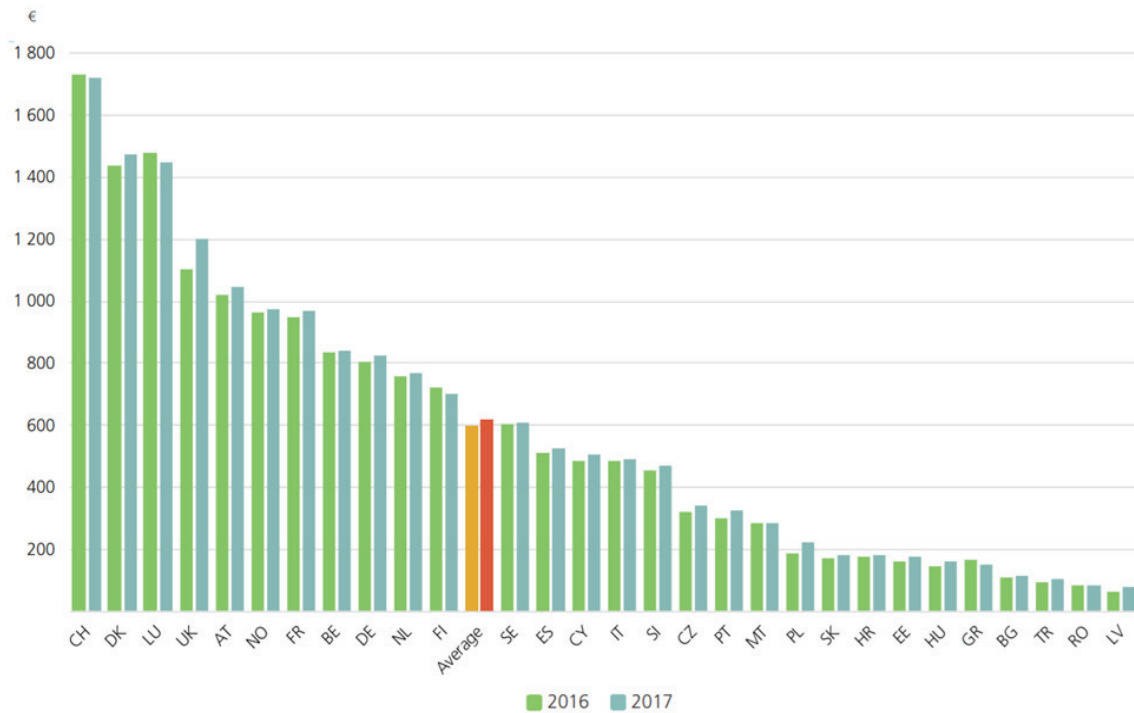


Fig. 8. P&C premiums per capita by country in 2016–2017 (€)

Source: European Insurance – Key Facts (2018: 21)

Unfortunately, it should be stated that by the volume of the written premiums related to P&C, Latvia is in the last place in this rating with a share of 0.6% (Figure 8).

3. Trends in Latvian insurance market development and non-life insurance services in Latvia

Participants of the risk insurance market. In Latvia, as in other countries, insurance companies that implement 7 life insurance types and 19 non-life insurance types are the insurance service providers (“Insurance and reinsurance law” of Latvia, article 19, 2015). Insurance types and the insurance market legal regulation are established by the laws of Latvia, which are based on the EU Directives on insurance. According to the Financial and Capital Market Commission data, 17 insurers were registered in Latvia in 2017 (Financial and Capital Market Commission LR (fctk LR), 2018). Six insurers are involved in life insurance, and all registered insurers represent European insurers (Latvian Insurers Association, 2018):

- “CBL Life”.
- “SEB Dzīvības apdrošināšana”.
- Compensa Life Vienna Insurance Group SE Latvijas filiāle.
- ERGO Life Insurance SE Latvijas filiāle.
- Mandatum Life Insurance Baltic SE Latvijas filiāle.
- Swedbank Life Insurance SE Latvijas filiāle.

Under Latvian law 11 insurance companies are engaged in non-life insurance or, as commonly cited “insurance other than life insurance”, according to the EU Directives, four domestic insurance companies function in Latvia:

- “Balta”.
- “Baltijas Apdrošināšanas Nams”.
- “BTA Baltic Insurance Company”.
- Seesam.

The remaining 7 insurers are registered branches of European insurance companies:

- Balcia Insurance SE.
- “Compensa Vienna Insurance Group” ADB Latvijas filiāle.
- Akcine draudimo bendrove “Gjensidige” Latvijas filiāle.
- ERGO Insurance SE Latvijas filiāle.
- If P&C Insurance AS Latvijas filiāle.
- If P&C Insurance Ltd (Publ) Latvijas filiāle.
- Swedbank P&C Insurance AS Latvijas filiāle.

Pursuant to the Financial and Capital Market Commission report (Public quarterly reports Financial and Capital Market Commission LR by insurers, 2017) If P&C Insurance Ltd (Publ) Latvijas filiāle companies are listed as inactive based on 2017 reports.

Based on the Financial and Capital Market Commission report (Public quarterly reports Financial and Capital Market Commission LR by insurers, 2017), calculations and analysis of the insurance sector financial index for the insurance market in Latvia were executed, namely a market share of each insurance company and the concentration factor.

Market share specifies the insurance company position in the market in relation to competitors. The calculation formula (1) is applied for this purpose (Novozhilova, 2012):

$$D_i = \frac{P}{V_{2017}} * 100\%, \quad (1)$$

where D_i – share of market;

P – gross-premiums, mln. EUR;

V_{2017} – capacity of insurance market in 2017, mln. EUR.

Market potential means the total scope of liability that insurance companies involved in insurance, co-insurance and reinsurance of a certain risk can assume based on their financial capabilities.

The market capacity in Latvia $V_{2017} = 646.15$ mln. EUR (Calculate according Public quarterly reports Financial and Capital Market Commission LR by insurers, 2017).

In terms of gross premiums, BTA insurance company with the premium volume of EUR 162.97 mln. EUR (Public quarterly reports Financial and Capital Market Commission LR by insurers, 2017) and market share of 25.2% became the market leader in non-life insurance segment, it is followed by Balcia with a share of 15.2% and BALTA with a share of 13.7%. The market concentration ratio (CR) (three leaders of the market) represents the percentage ratio of gross-premiums of the societies having the most significant shares in the market relatively to a general amount of gross-premiums and is calculated by formula (2) (Novozhilova, 2012):

$$CR = \frac{\sum^m Q_k}{\sum^m Q_k + \sum^n Q_j}, \quad (2)$$

where CR – market concentration ratio;

Q_k – amount of k -larger insurance society of gross-premiums;

Q_j – amount of j -smaller insurance society of gross-premiums;

m – number of the largest (by market share) insurance societies of gross-premiums;

n – number of smaller (by market share) insurance societies of gross-premiums.

Hence, the market concentration makes 54.03% and is determined by three companies.

Determination of the risk insurance market share in Latvia. Market potential by insurance type must be considered for the year in order to determine the market share. As a result of data analysis (Public quarterly reports Financial and Capital Market Commission LR by insurers, 2017), the authors have determined that the non-life insurance sector in Latvia accounts for 82% of the written premiums market (Figure 9).

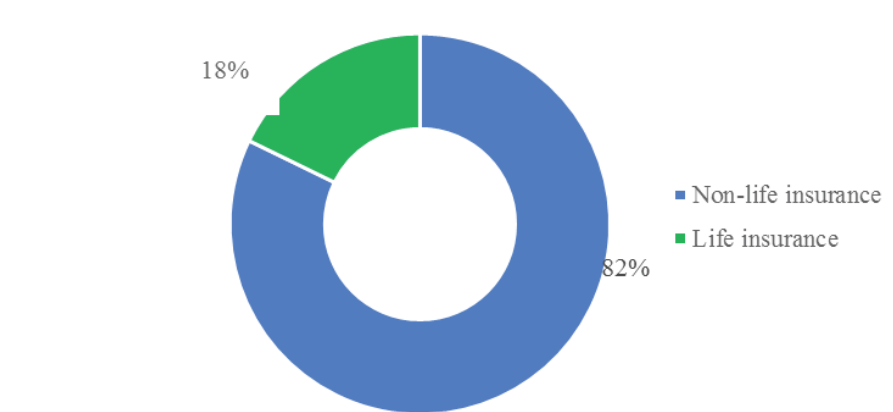


Fig. 9. Insurance market structure in Latvia in 2017

In Figure 10, there is presented data of comparative analysis of the European insurance market structure (Figure 3, Section 2) between the index related to similar insurance types in Latvia: life, health, motor, property, general liability, casualty, other (constructed according to Public Quarterly Reports Financial and Capital Market Commission LR by Insurers, 2017).

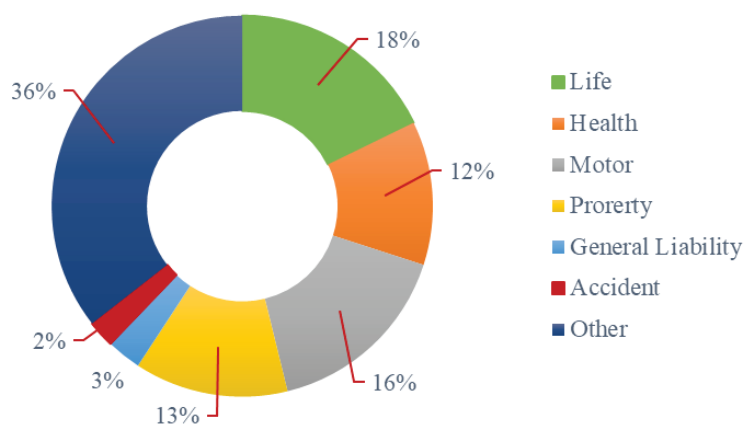


Fig. 10. Structure of written premiums insurance market in Latvia in 2017 by types that are similar to insurance market structure in Europe (%)

Loss ratio is an important index of the insurance market. This index enables to evaluate, what part of the received funds an insurance company should allocate for payments. It is calculated as the ratio of all payments sum for a particular period to the collected insurance premiums sums for the same period of time (Novozhilova, 2011). This index is analysed both in the general form and in the ratio for each insurance type at the risk insurance market.

The loss ratio factor is determined by formula (3) (Novozhilova, 2011):

$$L = \frac{\sum B}{\sum P} * 100\%, (3)$$

where

- L is the payout level in %.
- B is the amount of redemption for this insurance type for the reporting period (total Gross claims paid).
- P is the amount of payments for this insurance type for the same period (total Gross premiums written).

Since the numerator and denominator of this index are included in the reporting data of the Financial and Capital Market Commission and are published in the press, the findings on this index is of interest for all insurance market subjects.

The value of the loss ratio index depends on the insurance market development level. If the value $l > 1$, it indicates that a company more gives than receives, spending its own capital. In this case, it also applies to the insurance types under consideration (Novozhilova, 2012).

Figure 11 presents the authors' calculations of the loss ratio factors by the insurance types in Latvia in 2017 (calculated according to the Public quarterly reports Financial and Capital Market Commission LR by insurers, 2017).

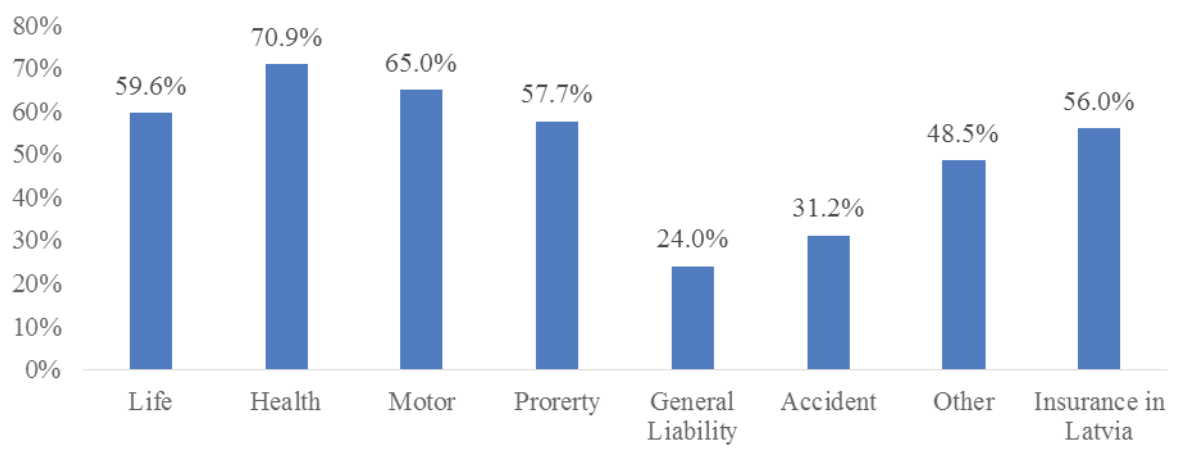


Fig. 11. Loss ratio factors by the insurance types in Latvia in 2017 (%)

The authors' calculations of the loss ratio factors in Latvia show 56% (Figure 11), whereas in the world – 84%.

If the loss ratio is less than or equals to 50%, this fact indicates the profitability of the insurance type, but herewith the loss ratio related to the compulsory insurance of automobile owner civil liability is considered conventional even at the index equal to or greater than 60% (Novozhilova, 2012).

Therefore, the authors underline several distinct (important) features and differences in the data comparative analysis:

- Share of life insurance in Latvia is much lower in comparison with non-life insurance, more than 4.5 times. This type is not as demanded as non-life insurance. The same trend is noted in different reports related to the insurance market and in other less developed markets in the world. Life insurance policies in Latvia are not assigned the securities status under which loans and credits can be issued, as in countries with developed and stable economy. The negative attitude to accumulative insurance types throughout the post-Soviet space, due to the “loss” of savings at the USSR collapse – the human factor – should be considered as well;
- In motor insurance, the auto-CASKO group’s share is proportional to the European market. The sector of this insurance type in Latvia is larger by 5% than in Europe. This provision may be stipulated by a significant share of transport procured under leasing contracts, where CASKO insurance under the contract terms is mandatory;
- The property sector of the insurance market in the EU and Latvia (as well as auto – CASKO) are proportional to the general trend, but with an excess of 4%. The basic reason is a significant number of loans in Latvia, charged upon property. Under the loan contracts the mortgage insurance is mandatory.
- The most significant difference is found in the other group (Europe – 5%, Latvia – 36%). The Latvian data in this market share determination include the insurance type of the motor vehicle third party liability compulsory insurance. It is a compulsory insurance type and it, perhaps, must be withdrawn from comparative data. Similar analysis of the insurance market without considering this insurance type approximates the market distribution trends to the European one. The compulsory automobile owner liability insurance in Latvia is included in the significant type list with a share of 13.52%, so the index imbalance is observed.

Conclusions

The research findings confirmed the unification of the global, European and the Latvian insurance space. European and Latvian markets are regulated and operated based on the EU Directives. Insurance products and the insurance market structure in Latvia reflect general development trends. The difference is observed in the life insurance sector, which is stipulated by economic and historical reasons. The Latvian non-life insurance market is harmonized sufficiently with the European one and is developing with similar trends. The analysis revealed high concentration of non-life insurance market in Latvia (54.03%), which is determined by three insurers, and this situation adversely affects the market development. Due to business insurance coverage provision, the choice of insurer – Latvian or European one for a particular insurance type – is especially significant. This work constitutes the initial stage in preparation for the analysis of the insurance market of the transport sector for insurance logistics implementation in the enterprises executing international cargo carriage.

The findings can be used by insurers and entrepreneurs for the insurance coverage advanced planning and for ensuring business risk management of the company.

As a result of the analysis carried out by the authors, it is reasonable to recommend to Latvian entrepreneurs to use guaranteed insurance protection implemented by the Latvian insurers. It would help to implement the risk management program, since the trends and development principles of the Latvian insurance market are provided by the presence of the leading European insurers and comply with the modern EU directives.

Finally, the authors suggest using the findings of the study of the insurance market in the transport insurance sector for development of the carriage enterprise logistics insurance.

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DABARTINIŲ DRAUDIMO RINKOS TENDENCIJŲ LATVIJOJE ANALIZĖ

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Santrauka

Straipsnyje nagrinėjamos dabartinės pasaulio, Europos ir Latvijos draudimo rinkų tendencijos. Draudimas leidžia sumažinti ir likviduoti ekonominius nuostolius, kurių atsirado dėl nepalankių įvykių. Draudimas – tai vienas veiksmingiausių įmonių rizikos valdymo būdų. Verslininkas turi būti informuojamas apie siūlomas draudimo paslaugas, draudimo rinkos dalyvius ir draudimo rinkos valstybę užtikrinant draudimo apsaugą. Ši informacija padės tinkamai pasirinkti draudimo apsaugą, siekiant užtikrinti įmonės finansinį stabilumą.

Tyrimo tikslas – nustatyti draudimo apsaugos atitiktį dabartiniams ES reikalavimams ir galimybę įgyvendinti Latvijos įmonių rizikos valdymo programą, remiantis ilgalaikę ir trumpalaikę draudimo rinkos perspektyvos analizę pasaulyje bei Europoje.

Užduotys: nustatyti ir apibūdinti bendrąsias surinktų draudimo įmokų (realios priemokos augimo) apimties tendencijas pasaulinėje draudimo rinkoje ilgalaikėje perspektyvoje; išanalizuoti Europos draudimo rinkos būklės įvertinimo finansinį indeksą (nuo 2018 m. pradžios), pateikiant trumpalaikių perspektyvų prognozę; nustatyti draudimo rinkos raidos tendencijas, pagrįstas surinktomis draudimo įmokomis (realiu įmokų augimu) ir ne gyvybės draudimo paslaugų apimtis Latvijoje.

Objektas – ne gyvybės draudimo paslauga. Autoriai analizuoja finansinės veiklos rodiklius ir atlieka jų palyginamąją analizę, nustato bendrąsias tendencijas ir esamus draudimo rinkos plėtros skirtumus pasaulyje, ES ir Latvijoje. ES ir Latvijoje analizuojama draudimo rinkos struktūra bei gyvybės draudimo sektoriaus apimties skirtumai. Pateikiamas draudimo rūšių, Latvijos draudimo rinkos dalyvių ir draudimo rinkos būklės aprašymas. Analizės išvados gali remtis draudikai ir verslininkai, kad būtų užtikrinta draudimo apsauga Latvijoje.

PAGRINDINIAI ŽODŽIAI: *draudikas, gyvybės draudimas, ne gyvybės draudimas, realus įmokų augimas.*

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