Romanian Insurance Market Facing Globalization Process

■

Dumitru G. Badea
Laura Elly Novac
Academy of Economic Studies, Bucharest

Abstract. *The Romanian insurance market has passed through a permanent process of growth which ended up in 2004 to exceed the threshold of 1 billion Euros, in the frame of a small awareness and confidence of the population towards insurance, even now after 15 years. The globalization process of the financial markets affected also the Romanian market even before Romania became member of the European Union. The globalization brought about benefits (especially under the form of increase in the quality of the services provided to clients) but also disadvantages for local companies (significant costs in logistics and training in order to cope with the international groups).*

Key words: globalization; mergers; solvency; capitalization.

■

JEL Codes: F01, G22.
REL Codes: 11C, 10J.

Introduction

Although the insurance activity is well known to the Romanian market ever since the 14th century, when insurance was all about mutual help, this activity evolved rapidly in the period before the First World War and in the period between the World Wars, and it manifested itself as the entrance on the market of insurance companies representatives from countries as Austria, Italy, Great Britain.

The offered insurance services related to cargo insurance, fire insurance and life insurance. The protection against natural calamities (especially hail) was offered at a smaller scale and for a limited period.

In 1952, at the same time when nationalization started, the insurance industry was transformed into a state monopoly, thus only one company was active on the Romanian market, dealing mainly with the population involved in agriculture with the sole purpose of reassuring the authorities.

No foreign company had access to the Romanian market or had the right to bring capital in Romania, and the computations regarding the insurance premium or the insured amount were considered to be top secrets, known only by a small group of people that had succeeded in understanding these insurance secrets through training sessions outside the country.

ADMINISTRATIA ASIGURARILOR DE STAT (National Insurance Administration) – ADAS continued its activity under the management of the Ministry of Finance and offered mainly insurance services, reinsurance services and claims settlement services.

ADAS's object of activity was compulsory insurance (imposed by law) and facultative insurance. The *insurance imposed by law* offered by ADAS referred to general insurance for the assets that were the property of agricultural co-operatives and inter-co-operative associations (including their economic units), insurance of goods that were the property of natural persons, travel insurance against accidents, general liability insurance for damages from motor accidents. The *facultative insurances* offered by ADAS (in lei or foreign currencies) came to supplement the insurances imposed by law, and were insurance of property against average, destruction, theft or others; personal insurance for disabilities, death, survival or others; liability insurance for bodily harm, death, goods average or destruction and other damages for which liability was demanded by the law in force at that time.

The interesting fact is that the compulsory insurance share had a growing trend towards the end of the 80's, on the basis of a accommodation of the population to insure their assets (household, car) through facultative insurance, emphasized also by the increase rate of the insurance market which was grater than the growth rate of the general economy. Between 1955 and 1989, the volume of insurance premiums recorded by ADAS increased 14.4 times, whilst the national income grew 10.2 times.

In 1989 the change in the political system came about with significant changes in the insurance industry. Certain types of insurance which previously were compulsory became facultative (for example the household insurance became facultative – a decision that is still debatable if we think about the exposures that Romania has to natural calamities and also about the large amount paid to cover the damages of the uninsured persons, from the state budget as emergency funds) (Badea, 2008a).

From the point of view of the insurance market's offer, the year 1989 meant also the end of state monopoly, ADAS seized its activity and its portfolio was taken over by three companies that later on were privatized – ASIGURAREA ROMANEASCA SA (that took over the fixed assets of the former company, its main products – life insurance, compulsory insurance etc.), ASTRA SA (took over the external contracts), and CAROM SA (became responsible for the claims settlement, establishing the paid claims for averages generated in Romania), being set up through law in 1990.

The year 1991 represented a turning point, thus starting with this year the first insurance company with entirely private capital was founded, UNITA SRL, followed by a multitude of other organizational entities (with local or foreign capital).

The beginning of "the new era" for the Romanian market represents the year 2000 when the law concerning the supervision of the insurance market was implemented, and the Insurance Supervisory Commission was set up; better improvements have been registered.

Since then, the Romanian insurance market recorded a constant growth that could be summarized as follows: in 1997 there were 47 insurance companies that cashed in a total volume of premiums of 167.7 million Euros, in 2000, there were 73 insurers that recorded a total volume of 337.79 million Euros and in 2007 there were 42 insurers that succeeded in a total volume of written premiums of 2.15 billion Euros. The continuous improvement in terms of total volume of premiums, of insurance density and insurance penetration (as amount of euro paid, per capita, on average/year) come to support the idea of growing importance of this activity sector.

The continuous trend of increase of the Romanian market may be summarized in the following table:

Insurance market ratios

Table 1

		2000	2001	2002	2003	2004	2005	2006	2007
Number of insurers		70	47	45	40	40	39	41	42
Volume of subscribed premiums	Mil USD	311	344	500	610	1051	1508	1970	2630
Penetration degree	% GDP	0,85	0,87	1,09	1,06	1,44	1,55	1,67	1,84
Insurance weight	USD/capita	13,85	15,38	22,95	37,51	47,01	68,4	91,27	122,3

Concerning the last three years...

In 2006, the total volume of insurance premiums reached 1.62 billion Euros, a nominal increase of 23.68% compared to 2005, when the volume of premiums recorded 1.21 billion Euros, being the second year in which the threshold of 1 billion Euros was exceeded.

The 41 insurance companies active on the market brought about an average growth of the insurance market of 23.68%, more than in 2005, when the growth was only of 17.01%.

In 2006, the insurance density reached the level of 74.63 Euros/inhabitant as compared to 56.10 Euros/inhabitant in 2005. Of course, the biggest density was recorded in Bucharest, where, on average, a person spent 394.19 Euros (as compared to 281.23 Euros in 2005) (Rosca, 2008). The average density computed without taking into consideration Bucharest area reached a "staggering" level of 39 Euros/inhabitant.

The weight of general insurance represented 80.1% in total volume of insurance premiums (after 75.6% in 2005), stressing the trend of the Romanian population to be focused less on the life insurance and more on the insurance of their property.

In 2007, 42 insurance companies centralized a total volume of gross written premiums of 2.15 billion Euros with a nominal increase of 25.07% compared to the level of 2006. As structure, 79.9% of the total premiums was generated by the general insurance (an increase of 24.73% in the volume of premiums subscribed compared to 2006), whereas the life insurance brought about only 20.1% (a more accentuated increase – related to the increase in the general insurance – of 26.46% compared to 2006).

The insurance penetration for 2007 was of 1.84% (insurance premiums compared to the GDP), an improvement as compared to the 1.67% registered in 2006. As far as the average insurance premium paid by a Romanian is concerned, this ratio (the insurance density) recorded a level of 333 lei/inhabitant (compared to 266 lei/inhabitant in 2006).

Analyzing the distribution of subscribed premiums over the Romanian territory, in 2007, 44.76% of the total was generated by Bucharest, followed by Northern-West area (9.74%), South-East area (9.08%) and South area (8.62%). The insurance density in Bucharest reached in 2007 the level of 1440 lei (432.3 Euros)/inhabitant, all the other regions being under the national average, showing the development potential of the regions (between 140 lei/ inhabitant and 255 lei/ inhabitant) (Rosca, 2008).

The main types of general insurance required by the market in 2007 were the motor insurance (including the third party liability) – 72.1% and property insurance (11.3%) (Rosca, 2008).

The insurance companies *paid claims* that amounted more than 1 billion Euros during 2007. Thus, after the insurance industry overcame a turnover level of 2 billion Euros also the paid claims level exceeded 1 billion Euros, rising with about 35%, in comparison with the value of the same indicator recorded in 2006.

About 95% from the total amount of paid claims came from non-life insurance, meaning an absolute value about 950 million Euros, figure that represents more than 55% from the gross premiums written for non-life insurance. In a matter of fact, the insurance companies paid during 2006 more than half they had written.

The most significant share in the total amount of paid claims is owned by motor insurance for which the insurers paid about 726 million Euros, amount that represents 59% from the gross premiums written for the mentioned insurance class.

The total amount of claims paid for motor insurance exceeded 500 million Euros in 2007, rising with more than 32% as compared with the value of the similar indicator in 2006. The total amount of gross written premium from motor insurance reached approximately 800 million Euros rising with more than 42% than the results of 2006. In fact, the motor insurance owns about 37% from the insurance market and is causing more than 50% from the claims paid for the entire market (Hodorog, 2008).

The Romanian industry recorded in 2007, for the second consecutive year, a *negative financial result*, a net loss of about 253 million lei (approximately 75.8 million Euros), which reported to the total subscribed premium, of 7.17 million lei (2.15 million Euros), represents 3.5%.

This net loss was due to the fact that in 2007 the life insurance activity shrunk its net technical profit to 66 million lei (as compared to 106 million lei in 2006), and the general insurance activity recorded a net technical loss of approximately 324 million lei. Reported to the volume of subscriptions on the general insurance segment, the net technical loss recorder in 2007 in general insurance represented 5.7%, as compared with 3.7% in 2006.

At the level of European Union, the Romanian insurance market had in 2007 the fastest growth in the entire Europe, overcoming other significant markets in the region, such as Poland. With a growth rate of 33% in Euros, the local insurance market had the greatest dynamics among the 33 member states of CEA – Comite Europeen des Assurances.

In the last 15 years, the insurance market increased 30 times in terms of gross insurance premiums subscribed and even though the motor insurance continue to have a significant weight, it can be noticed an accelerated increase of other property insurance, credit insurance and health insurance.

The continuous improvement of the insurance premiums, the insurance density and the insurance penetration rate (annual amount of Euros paid on average by an inhabitant) support the importance of this sector of activity in the total economy of Romania.

The accession to EU brought about both benefits and costs for the insurance market. As the market became more sophisticated (the consumers became more informed and demanding), the offer became more stable, and the concentration of the market began to reduce itself as a response to the European insurers that entered our market.

New products were launched on the national market, supported by similar products offered on the European market; new services occurred for the consumers (risk consultancy, claims adjusting etc.); better transparency was recorded, due to supplementary requirements of the supervisory authority, as the insurance companies offered more information about their financial position for the consumers.

Other benefits refer to an improvement of the underwriting conditions and even the contractual relations with the international market (the reinsures) that resulted in smaller levels of the insurance premiums (Badea, 2008b).

The Romanian insurance market and globalization

Once the Central and East European insurance market was open in 1990 due to changes that emerged, there was a development on this market especially through the appearance of mixed companies or the opening of subsidiaries that belonged to international insurance companies.

The globalization of the insurance field is an already established fact due to the reinsurance relation that is mainly practiced at international level, completing the world level attraction that insurances have due to the establishment of large insurance groups with offices and subsidiaries in many countries.

The financial markets were linked even more tightly due to the globalization process. There are advantages but also disadvantages that accompany this process. A plus is that there is a better capital resource allotment. There are no more frontiers between markets. There is a need to establish an optimum mix between risks and results. These facts aid the convergence process. But there are side effects also, which are less desired. The exposure of players on an increasing globalized market brings about the appearance of a more complex risk system which is even harder to manage. Even more complex financial products are launched which present a level of opacity that makes more difficult the understanding of ever so complex risks, especially in periods of irrational effusiveness.

The Romanian insurance market cannot stay outside the globalization process.

Until 1989, in Romania, insurance was a state monopoly, Administrația Asigurărilor de Stat – ADAS being the sole institution in Romania to deal with insurance/reinsurance. After 1990, major legislative changes led to the disappearance of state monopoly and to the establishment of the competitional atmosphere on the Romanian insurance market.

Later on, companies with private, Romanian or mixed capital emerged (taking into account the fact that the Law did not allow the establishment of companies with 100% foreign capital).

The Romanian insurance market is going through a continuous globalization process. This process accelerated with the accession of Romania to the European Union. The Romanian insurance market is now part of the European insurance market, which is in itself going through a globalization process.

Since January 1, 2007, any insurer or authorized insurance intermediary from any other member state of the European Economic Space (EES) can conduct its activity in Romania, either directly or through a branch established in our country, without the need of further authorization from the Insurance Supervisory Commission. They must send a notice to the regulatory authority in Romania through which they must express their intention to extend their activity in our country.

Another method of entering on local market for foreign companies emerged within the framework of developing the activity of *bancassurance* (Bunea, 2002). Important banks with foreign capital, within the system, also established insurance companies: CR Asigurări de Viață SA and BCR Asigurări SA, ATE Insurance Romania SA, Carpatica Asig SA, OTP Garancia Asigurări SA, Societatea de Asigurare și Reasigurare City Insurance SA, Credit Europe Asigurări-Reasigurări SA.

As a result, the globalization process on the Romanian market is expected to accelerate.

The Romanian market could be dominated by a small number of insurers, as a result of offer *concentration* trends, due to the globalization process that is happening in Central and Eastern Europe, as a GfK

România market research shows (Ciuncan, 2008). The number of large insurers has decreased as a result of mergers and acquisitions at Central and Eastern European level – phenomenom that is just begining in countries such as Poland and Bulgaria.

The GfK România study used as benchmark the economic aspects from Austria, a country in which, starting with 1995, a market quota phenomenon was observed, as a result of big insurance companies mergers.

Over the years, the entrance of foreign insurance companies on the market was achieved with the establishment of companies in our country, through acquisitions and mergers.

In 2006, the weigh of the foreign capital on the Romanian insurance market was 62% and the local players were a rare sight, at least in the Top 10 (Ciuncan 2008); this weight is expected to increase even more, based on the large set of acquisitions and mergers.

2007 continued the process of acquisitions and mergers started in 2005, with big European insurance groups taking over local players – eg. the Czech investment group PPF Investments took over shares of RAI and ARDAF; the Austrian group VIENNA Insurance Group enhanced its participation on the Romanian market with ASIROM and AGRAS (alongside Omniasig, Omniasig Asigurari de Viata); EUROHOLD financial group took over ASITRANS company; UNIQUA strengthened its participation in ASTRA, becoming main shareholder; the Greek company Ethniki decided to merge by absorption two Romanian companies GARANTA and NBG Insurance; GROUP AMA took over BT Asigurari, OTP Garantia and ASIBAN (the latest two in 2008).

After the year 2007 was considered to be "The Monopoly Year", it is expected that the concentration trend of the insurance field will remain constant. In March 2008, the market was taken by surprise by the announcement of ERSTE Bank, which intends to renounce to its investments in insurance in the favor of Vienna Insurance Group (VIG). The number one in the top of volume of subscribed premiums, on the first trimester of 2008, with a market share of 30.4% (665 mil. Euros) wishes to give up UNITA in favor of the group UNIQA which will reach 11.8%, 4th place on the Insurers' top (Plăcintă, 2008), after only Allianz (17.3%) and GROUPAMA (12.9%).

This entrance on the European market came with major increases for the operators on the insurance market – foreign groups that entered on our market, in only 5 years, recorded 5 to 7 times increases (for example, VIG's market share recorded the biggest growth ever, 7 times the value it had in 2002 when it has 4.8%).

One of the important conditions imposed on the Romanian insurance industry regarding the basic requirements for the solvency criteria referred to the increase of the social capitals of the insurers (Novac 2008). As a result of these conditions imposed by the Insurance Supervisory Commission the social capital was increased by all the existing insurance companies, less 6 companies that were unable to succeeded in this endeavor and thus, their activities were terminated (ABG Insurance SA; Mediterranea Assicurazioni SA; Mondial Assurances SA; Nationala Companie de Asigurari si Reasigurari SA; Omniasig Addenda SA; Provitas SA). In 2007, half of the 42 insurance companies on the local market increased their capital with a total value equal to 153.5 mil. Euros – the largest increases were recorded at Omniasig (approximately 30 mil. Euros), Generali (22 mil. Euros) or Ardaf (approximately 7 mil. Euros) used for the development of the companies or to cover the losses caused mainly by the large damages from motor insurances.

Another important fact generated by the inclusion of the Romanian market into the European market refers to unitary evaluation norms of insurers. This is why we will mention the new *solvency system* Solvency II which imposes major capital increases. The Solvency II System represents the establishment of reserves for each risk category, in other words a correlation between assumed risks and the insurers' capital. More than this, since Solvency I is focusing on liabilities, which are represented by insured risks, the Solvency II System will focus on assets. Thus we will take into account risks such as credit or operational risks, which are not taken into account by the current system. Insurers have as deadline 2012 in order to implement this new system.

Conclusions

Globalization has linked the financial markets more and more in the last period. There are advantages, but disadvantages also. There can be sideslips, and there is only so little till a crisis is reached. Romanian insurers have reported major increases in the volume of assets but also relative weak increases for the net profit in 2007. The good results announced by the Romanian insurers did not have the strength to fight with globalization.

Both for our country and for other emergent countries, the national authorities together with the international community have to make possible a very assorted report between the economic adjustment and the economic development, between the costs and advantages of globalization. Thus the last resort for Romania is its integration in the globalization process (Crețu, 2005).

Through a careful regulation of the insurance market, Romanian market can reduce the globalization risks and can defend itself from the negative effects of this process. The affiliation to the European Union insurance market can aid to the accomplishment of this objective.

References

Badea, D. (coord.), Tudor, B., Novac, L.E. (2008). *Insurance agent's manual*, Editura Economică, București

Badea, D., „Romanian insurance market – benefits and costs after EU accession", International Conference of ASECU, Bucharest, 2008

Bunea, D., „Integrarea piețelor financiare și de asigurări", PRIMM nr. 4/2002, p. 10

Ciuncan, Al., „A rising star on the European map", *XPRIMM insurance & reinsurance*, p. 46. Nr.1/2008

Crețu R.F., „Libera circulație a capitalurilor în România, între globalizare și integrarea în Uniunea Europeană", în *Amfiteatru Economic* nr. 17, aprilie 2005

Hodorog A., „CSA: Piața asigurărilor s-ar putea tripla până în 2017, la 7,5 miliarde de euro", *Daily Business*, March 2008, București

Novac L.E., „Solvency II – cooperation at European level on the insurance market", *International Conference of ASECU*, București, 2008

Placintă A., „Uniqa preia Unita din fata competitorilor", Ziarul Financiar, nr.2400/30.05.2008, pg.1

Roșca A., „Profil teritorial: România 2006", *XPRIMM insurance & reinsurance*, Nr.1/2008, p.18, București