

Impact of Corona Crisis on Economic Development and the Situation in the Financial Sector of the Insurance Industry

Darina Móžiová¹

¹ University of Economics in Bratislava, Faculty of Business Management,
Department of Business Finance, Dolnozemská cesta 1, 852 35 Bratislava, Slovak
republic

moziova@gmail.com

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Abstract. The insurance industry has become one of the most important sectors of the national economy in the last decade and is actively involved in the functioning of the market economy. It interferes with the lives of citizens, the state, business entities and also plays a significant role in international trade. The insurance market is constantly evolving and adapts to the needs and requirements of insurance entities, as well as relevant legislation. Its importance for citizens and businesses is unquestionable. It helps them maintain a standard of living and economic stability and, in addition, gives them the opportunity to invest temporarily free funds. It is part of the financial market, which is affected by various risks, which certainly include the period of coronary crisis. In this paper I will examine how the corona crisis until 2020 affected the insurance industry.

Keywords: insurance, coronavirus crisis, risk, insurance

JEL classification: G20, G21, G22

1 Introduction

The current insurance industry can be considered a relatively developed sector of every national economy in Europe. Historical development of insurance was closely related to the development and needs of human society. Observing uncertainty and risk, they began to seek to minimize the potential impact of these risks. It was precisely uncertainty and risk that led to the creation of insurance, and thus to the creation of a separate branch that deals with insurance.

According to the latest annual report of the NBS (2019), 14 insurance companies with registered offices in the Slovak Republic operated on the Slovak financial market under the Solvency II regime. As at 31st December 2019, one insurance company ceased to exist as a result of a merger with another insurance company. During 2019, one insurance company ceased its activities, and its insurance portfolio was transferred to another insurance company. In 2019, there were 20 branches of insurance and reinsurance companies based in another EU Member State on the territory of the Slovak Republic. According to the NBS, the slowdown in the global economy continued in 2019 during the financial market, the first signs of which began to materialize in the previous year. The economic environment was accompanied by growing risks stemming from global uncertainty from the effects of the trade conflict between the world's two largest economies (the United States and China) and the course of negotiations on the United Kingdom's withdrawal from the EU.

The decline in production mainly affected the industrial sector, which paid for the reduced demand for investment products. The absence of foreign sales hampered industrial production in particular - it has been declining continuously on a year-on-year basis since the end of 2018. Slovakia, like most EU countries, was at the peak of its growth phase and its growth rate slowed down considerably. The cooling world demand thus gradually ended the expansion phase present in the recent period in most European countries. The development of the economies of trading partners, especially Germany, on which Slovak exports depend, had a negative impact on the Slovak economy. The consumption of Slovak households continued to grow due to the continued favorable development of the labor market and the strong growth of the average wage, but its contributions to economic growth were no longer as strong as in previous years.

In 2019, the financial sector of insurance companies faced several long-term risks. The first risk is lower-than-expected asset returns, as a result of which insurance companies have been forced to close reserves. This had a negative effect on their profitability. The second risk is a new tax in the non-life insurance segment, which reduces profits and, in some segments, client demand, which has slowed down premium growth. This further highlights the problem of long-term loss of car insurance. A significant structural risk is that a large part of own funds is formed by the volatile component of expected profits from future premiums, which cannot effectively cover possible sudden unexpected losses. Although the share of this component has decreased slightly, it remains the highest in the EU.

According to the analysis of OVB Allfinanz Slovensko, in 2020 the Slovak insurance market fell by 3%. That's according to a study by the Allianz Group. According to them, this negative development can be fully attributed to life insurance, which represents only 40% of premium income and fell by as much as 10%. On the contrary, insurance in the property segment increased by 2.4% and the reason could be the price competition.

2 Methodology

This paper evaluates the impact of the coronavirus crisis on economic development and the situation in the financial sector of the insurance industry. To obtain the necessary information and data, a survey method was used through statistical data obtained in the Slovak Insurance Association and their comparison with the period before the coronavirus crisis. Data for written premiums, including active reinsurance for all insurance companies and branches in the Slovak Republic, and claims incurred were used for comparison and analysis. The result is the Technical Result, which, by comparing the years 2019 and 2020, shows how the insurance company managed claims in its portfolio during the crisis. The financial result talks about how insurance companies handled reserves and how they were able to increase their value, and combined result talks about the percentage of non-life insurance and active reinsurance contributing to this result. Comparing the years 2019 and 2020, we will find out the impact of the coronavirus crisis on economic development and the situation in the financial sector of the insurance industry.

3 Current situation in the financial sector of the insurance industry

The insurance market is a special type of market in which supply and demand in the field of insurance and reinsurance take place (Majtánová, 1998). Insurance as a non-productive sector of the national economy is one of the most important sectors of each state. They are part of the financial market, located as a special branch of financial services that are provided to businesses, citizens and companies. The importance of insurance lies in the fact that it helps to stabilize the economic situation in society and creates new job opportunities (Meluchová, 2000). If the economy is balanced and successful, then the insurance market is also credible. Developments in the insurance market are leading to greater complexity of services and new forms of communication with the client. The globalization of the world economy facilitates the achievement of these goals, but multiplies the risks. The financial market represents a system of economic relations and institutions mediating the allocation of free funds (Koščo, 2002). In terms of individual segments, the financial market is divided into:

- Money market,
- Capital market,
- Foreign exchange market,
- Commodity market - market with precious metals and other commodities,
- Insurance market - insurance and reinsurance market.

The financial market can be broken down according to different aspects and criteria (Figure 1). Each division of the financial market is always a certain simplification and does not allow to include the financial market in its complexity and interrelationships. We encounter the division of the financial market with several authors, such as Kudzbel (1999), Čejková et al., (2002), Majtánová (2009). According to the mentioned

literature, we distinguish the financial market from two points of view - in terms of time and in terms of a segment. According to Kudzbel, we can define the insurance market as follows:

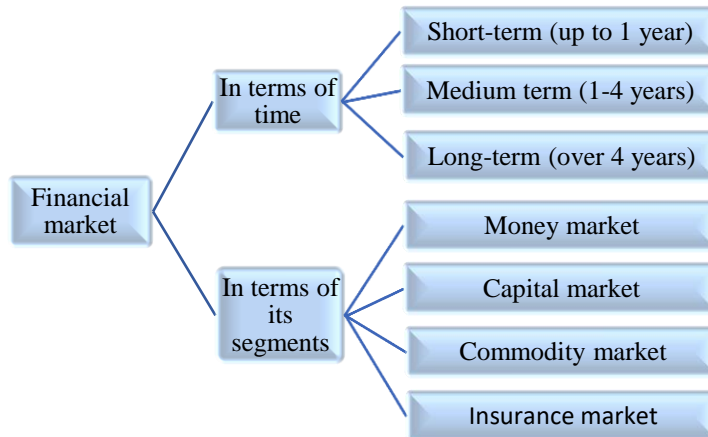


Figure 1 Financial market breakdown

Source: Own processing

The basis of insurance is the objective existence of risk. Reducing this risk should be a natural human endeavour. If we understand the population as the basic subject of the insurance market, we will find that insurance is at its lowest level on its personal scale of consumption. It should be emphasized that the ratio of life and non-life insurance in the developed EU countries is approximately the same. The situation on the world insurance market is influenced by the processes that determine the state of the world economy. At present, it is a relatively high rate of overall economic growth, accelerating international trade in goods, increasing production capacity and expanding the purchasing power of the population. The activity of insurance markets in developing countries is also increasing, but above all the situation on national insurance markets in the most developed countries of the world. The characteristic determinants of the world insurance market are:

- Further development of insurance,
- The ongoing process of capital concentration,
- Ongoing internationalization of insurance.

The insurance market can be defined according to the subject of business, the subject of insurance and reinsurance or according to the entities that influence it. The subject of insurers' business is insurance activity, reinsurance activity, preventive measures, broker activity and insurance-related activities, which serve to support and develop the insurance industry as well as to expand and improve insurance services. Insurance activity includes underwriting business activity, which consists in negotiating insurance contracts; administration of concluded contracts and collection of premiums on the basis of concluded insurance contracts; liquidation activity, the aim of which is to determine the size of claims incurred, valuation of damages, determination of size

claims and the payment of claims and the actuarial and technical activity, which includes the determination of the size of premiums and the size of insurance reserves. Reinsurance activity represents the vertical spread of risk in connection with risk diversification. By preventive activity we mean the prevention of damage. This is carried out by prefinancing individual preventive measures from the funds of the damage prevention fund, educational activities leading to the limitation of risk realization or by various elements in the construction of certain types of insurance (Vávrová, 2013). According to the subject of insurance and reinsurance, the insurance market is divided into life insurance, which is focused on the risk of survival or death, and non-life insurance, which is focused on various risks in property and liability insurance. Entities influencing the insurance market are commercial insurance companies, clients (policyholders and insured), reinsurance companies, insurance and reinsurance intermediaries, the state, insurance supervision, associations and other insurance market entities (Čejková et al., 2011).

The investment insurance market operates in such a way that insurance companies invest their technical provisions in the financial markets. Life and pension insurance is usually associated with a long-term savings process and therefore the means of technical provisions are suitable for long-term investment in the capital market. Provisions in the non-life insurance sector, on the other hand, are associated with a short period of time in which they must be liquid (Vávrová, 2013).

We can divide the insurance market according to several criteria. The decisive criterion for division or segmentation is the subject of the insurer's activity, others may be insured risks, the subject of insurance, insurance products, insurance subjects, insurers and the like. The basic segmentation of the insurance market is shown in Figure 2 (Čejková, Nečas, 2008).

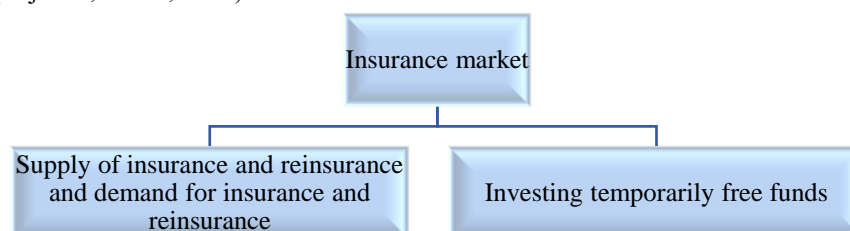


Figure 2 Basic segmentation of the insurance market

Source: Own processing according to (Čejková, Nečas, 2008).

Developments in the insurance market are influenced by several determinants. We can define them as external and internal.

External determinants affect developments in the external insurance market and include mainly the development and volume of gross domestic product (GDP), inflation, unemployment, population number and structure, life expectancy, breakdown into men and women, etc., monetary income of the population, or average wage, volume of household income and expenditure and their structure and situation in other segments of the financial market. Basic macroeconomic variables such as the development and volume of gross domestic product, the development of monetary

income, inflation and the development of unemployment affect the economic environment in which insurance and reinsurance companies operate and operate, and thus the activities and behaviours of insurance market participants. The population, the monetary income of the population as well as the amount of income and expenditure of households allow insurance and reinsurance companies to better estimate the scope and possibilities of their business or to adapt to the specifics, needs and insurance interests of the population. The situation in other segments of the financial market mainly affects the investment of free funds of insurance companies in the financial market and often has a significant impact on the state of management of insurance and reinsurance companies (Čejková et al., 2011).

Internal determinants influence developments in the insurance market from within and include mainly insurance, reinsurance and other related activities performed by commercial insurance and reinsurance companies, interest in insurance created by policyholders and policyholders, understanding of the importance of insurance by clients, insurance market regulation by insurance supervisors, the activities of insurance and reinsurance intermediaries and the activities of various associations. By the activity performed by insurance companies on the insurance market, we primarily mean offering and selling insurance. Reinsurers, in turn, enter the insurance market if insurers show interest in reinsurance. They therefore divide the existing risks into more entities, thus expanding the capacity of insurers. The supervisory authority shall issue an authorization to entities to carry on insurance and reinsurance activities, thereby carrying out its main, authorization activity. In addition, it monitors compliance with laws and legal norms, thus protecting the rights of policyholders. Intermediaries in the insurance market are an intermediate link between the insurer and the insured, resp. policyholder. They also provide their clients with services in the area of risk management, consulting, etc. Associations of insurance companies, insurance and reinsurance intermediaries and other associations represent their members, protect their interests and rights (Čejková et al., 2011).

The level of the insurance market can be characterized by several indicators that assess the efficiency of the use of resources and funds spent. These include, in particular, written premiums, claims incurred, claims paid, insurance market penetration and insurance market density (Čejková et al., 2005).

Premiums written, which means premiums that are set for the agreed insurance period or for the entire insurance period. It is an accounting list of all premium items that are to be paid to the insurance company at a given time. It is an indicator of the performance of each commercial insurance company for the relevant period and its amount determines the insurance company's share in the insurance market of the respective state and, after deducting costs, represents the basis for calculating the insurance company income tax. Premiums written are divided into life insurance premiums and non-life premiums written (Čejková et al., 2005).

The indemnity is calculated and provided by the insurance company for compensation of damage, claims paid, or part of the damage caused as a result of an insured event in non-life insurance or the agreed sum insured in the policy, the purpose of which is to obtain this amount. The insurance company is obliged to provide the insurance indemnity to the insured or the injured party in the event of an insured event

that meets the conditions agreed in the insurance contract, or specified in the law (Vávrová, 2013). We divide it into insurance benefits for life and non-life insurance. In the case of non-life insurance, it is not certain whether a premium will occur event, resp. how many times it occurs, but the insurance indemnity is provided only in the event of its occurrence (Vávrová, 2013).

The claims ratio represents the ratio between the amount of provided insurance indemnity and the amount of written or received premium. It is given as a percentage. It should be lower than the net premium (part of the premium tariff, which is intended to cover the insurance company's expenses for insurance benefits, including the creation of reserves) (Ducháčková, 2015) in percent and should not reach the full amount of premiums received (Vávrová, 2013).

Insurance penetration is one of the most important indicators of the development of the insurance market. It expresses the ratio of written premium to gross domestic product. It is also expressed as a percentage and in advanced economies it expresses the capacity of the insurance market. The total possibility of insurance on a given insurance market is given by the scope of the insurance field. An insurance field is a set of property, objects, persons or other phenomena existing in a given state or territory that can be insured and the insurance policy reflects the ability of the insurance market to cover the given field (Vávrová, 2013).

Insurance market density represents the share of the largest commercial insurance companies (usually five or ten) in written premiums. It is usually monitored for the 5, 10 and 15 largest insurance companies in the affected market (Vávrová, 2013).

We also know additional indicators, which include in particular the number of commercial insurance companies (indicates the development and maturity of the insurance market and the method of its regulation), number of employees in insurance, number of insurance contracts, average premiums per insurance contract, number equipped insurance events, etc. (Vávrová, 2013, pp. 38-39). The number of commercial insurance companies can document not only the development and maturity of the insurance market, but also the way it is regulated by the state. The number of employees in the insurance industry informs us about the level of the insurance market in terms of its staffing and human resources. The number of concluded insurance contracts expresses, among other things, the efficiency of commercial insurance companies, the average indemnity per insurance contract expresses the average indemnity of a commercial insurance company per insured event and the number of settled insured events expresses the final effect of insurance and thus the settlement and payment of the amount. the injured party is entitled under the concluded insured contract (Čejková et al., 2011).

4 Results and Discussion

The coronavirus crisis significantly affected economic development and the situation in the financial sector. The most significant event in the first half of 2020 was the outbreak of a coronavirus pandemic, which also hit Slovakia hard. Massive restrictions have been adopted to slow its spread. These restrictions have caused a sharp economic

downturn and a deterioration in the financial situation of many households and businesses. In the insurance industry, the coronavirus crisis was manifested mainly by a decrease in premiums written in life insurance, a decrease in the financial result and a reduction in the cost of claims in both life insurance and motor insurance. The development of written premiums for the period from 2016 to 2020 (according to SLASPO) is presented in Figure 1.

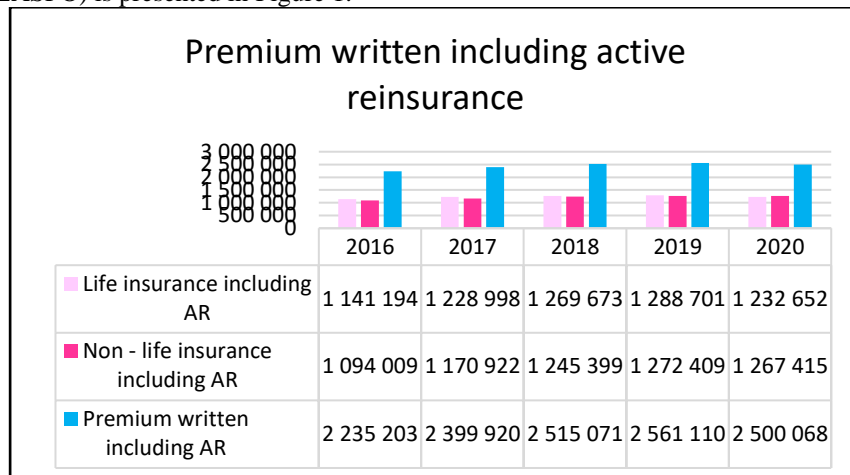


Figure 1. Gross premiums written 2016 - 2020

Source: Own processing

Total written premium decreased by 2.37% in 2020, which was mainly caused by a decrease in life insurance (-4.35%).

Graphically, the development of claims costs for the period 2016 to 2020 is shown in Figure 2.

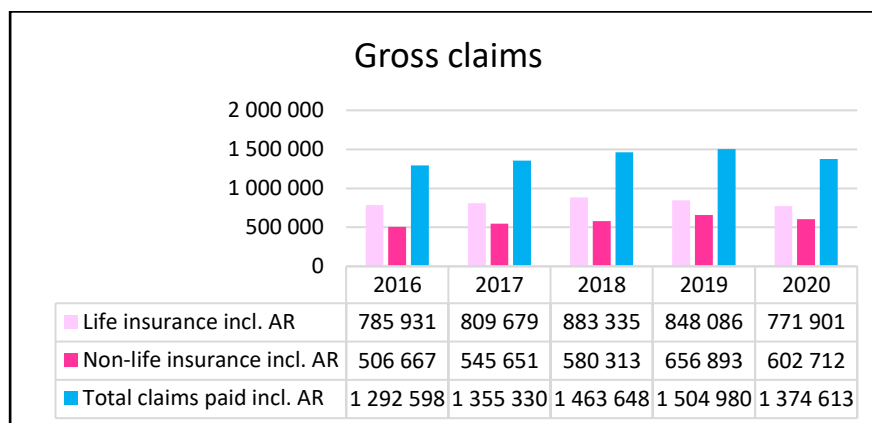


Figure 2. Gross claims 2016-2020

Source: Own processing

The technical result reveals how the insurance company managed to manage. It therefore represents the difference between the premiums received and the claims paid, together with other costs. Graphically, the development of claims paid for the period 2016 to 2020 is shown in Figure 3.

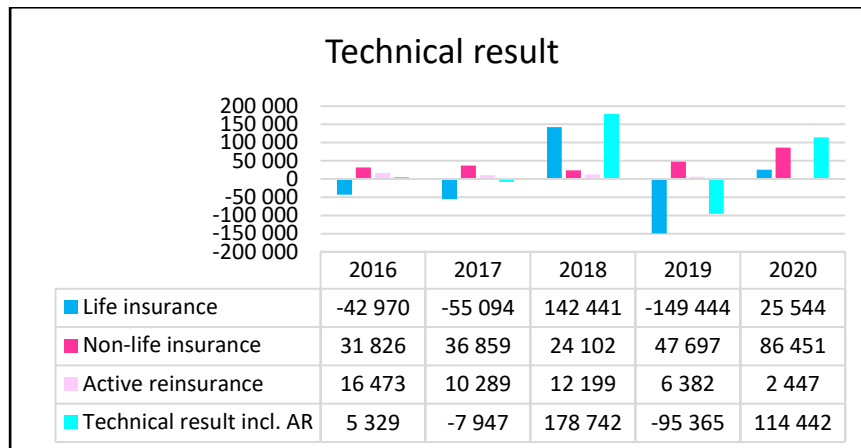


Figure 3. Technical result of insurance companies for the period 2016 to 2020

Source: Own processing

Graphically, the financial result of insurance companies for the period 2016 to 2020 is shown in Figure 4.

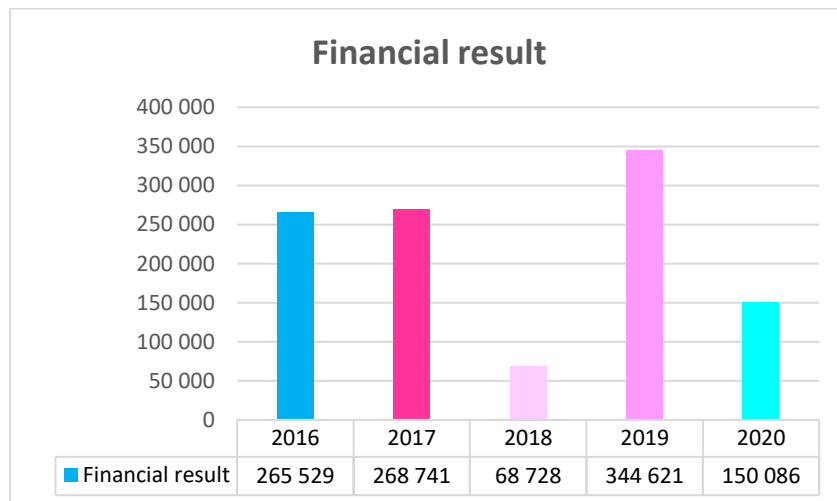


Figure 4 Financial result of insurance companies for the period 2016 to 2020

Source: Own processing

The financial result represents how insurance companies handled reserves and how they were able to evaluate them. According to Table 7, the financial result in 2020 is 56.45% lower than in 2019.

Graphically, the combined result of insurance companies for the period 2016 to 2020 is shown in Figure 5.

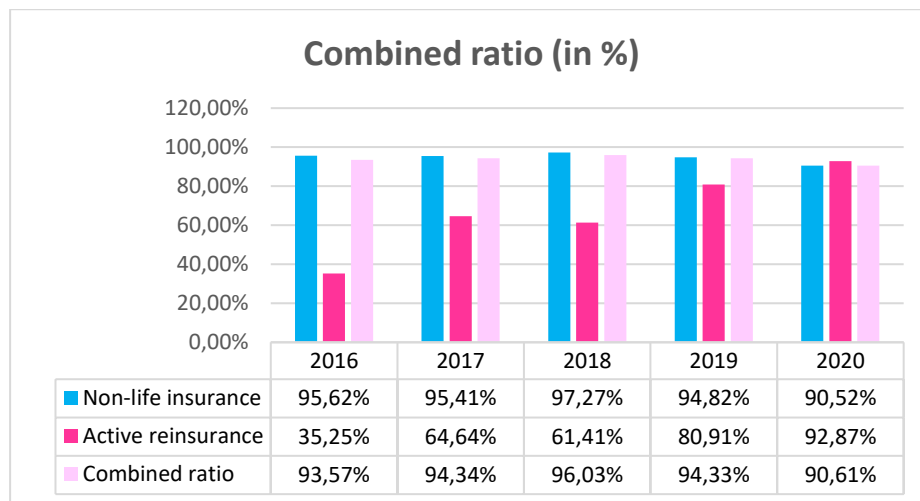


Figure 5. Combined result for period 2016-2020

Source: Own processing

The combined result talks about how non-life insurance and active reinsurance contributed to this result. According to Table 8, the decrease in the combined (-3.93%) indicator is due to a decrease in non-life insurance, which is 4.53% lower in 2020 than in 2019.

5 Conclusion

Insurance is an important sector of the economy especially in developed market economies. Therefore, observing its development becomes essential not only for entities operating in the insurance market, but also for entities operating in other segments of the financial market. Its development also substantially affects those interested in insurance and therefore not only corporate but also retail clients and thus has a certain impact on all market subjects.

In 2020 the insurance industry collected less written premium than in the previous period, but overall, it was more profitable. This is shown by the data of the Slovak Association of Insurance Companies (SLASPO) provided in this contribution. However, the insurance industry generated a profit of more than EUR197.7 million in Slovakia last year. In 2019, the profit of insurance companies, reinsurance companies

and branches of insurance companies reached less than EUR 182.7 million. The increase of taxed profit by around fifteen million euros means its increase of 8,25 %.

Insurance companies have significantly improved the results of insurance itself. The technical result of the insurance came to positive figures in 2020, when the sector generated a profit of EUR 114.4 million in this case. Non-life insurance contributed more than EUR 86 million to this result.

Based on the above, it can be concluded that the corona crisis has an impact on companies in Europe, including Slovakia, facing a decrease in their business revenues as a result of the coronavirus pandemic. However, the crisis did not affect all companies equally, with only 54% negatively affected. This was shown by Euler Hermes' survey, which was carried out among European clients at the end of the summer in order to obtain key information on the evolution of their turnover. Up to 20% of customers said their business was not affected at all and 19% even achieved an increase in sales.

However, it has been observed that insurers are reducing or eliminating any potential coverage for pandemic risk in property damage and business interruption policies. This creates a room to discuss the ability to transfer risks to the financial market and the of the government.

Based on the analysis, it can be concluded that the corona crisis, so far, has not impacted the insurance industry in the Slovak Republic substantially.

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