ISSN 2537 – 4222
ISSN-L 2537 – 4222

SOCIO-ECONOMIC VALENCES OF INSURANCE

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Abstract. *One of the main concerns of economists is economic growth. In this paper we show that insurance is an instrument for influence economic growth. Also, we analyze the impact of social and economic factors on insurance sector development. Thereby, this paper shows that insurance and economy are two correlated dimension. The development of national insurance markets, especially life insurance sector, allows us to promote financial stability, to improve welfare, to develop business and innovation. At the same time, insurance helps government to improve the social security and to strengthen national budget. Al of this effects leads to GDP growth. The results of this paper could be useful for governments, especially in emerging countries, to improve economic growth by stimulative policies for the development of insurance industry.*

Keywords*: insurance, economic growth, investments, saves.*
JEL Classification*: G22, O43.*

1. Introduction

Insurance industry is no longer seen as just a simple instrument for risk management, but is a complex force that contributes to the evolution of economic processes. By insurance, the savings are channeled to investment projects which are the main driving force for state development. The processes that take place in a country have effects on insurance market development. In this article we tried to show the valences of these interdependences and to demonstrate that insurance promote economic growth. On the other hand, insurance is influenced by the effects of some human activity processes such as demographics, psychological, politic and other factors.

To achieve the objectives of this paper, we started with literature review. It helps us to analyze existent studies and to estimate how the problem has been described. After that we divided the article in tree scientific compartiments. First is based on the description of the role of insurance in a country. Followed by chapter in which we determined the factors that have an influence on insurance sector. In the third part of this paper we analyzed the impact of insurance on economic development. As a result of investigations, we elaborated an outline description of financial circuit, involving insurers, which emphasize the role of the insurance industry in the economic system of a country.

2. Literature review

The first studies that highlighted the importance of insurance in an economic system were performed by Yaari (1965). He has been approached the problem of life insurance demand when uncertainty exists, the uncertainty named life span of a consumer.

Later Ward and Zurbruegg (2000) examined the relationship between economic growth and insurance market activity across nine OECD countries over the 1961 to 1996 period. They used real GDP as a measure of economic activity and insurance premiums as a measure of insurance activity and have established a long-time connection between these two dimensions. The authors used in studies the explanatory variables as private savings rate, budget surplus, population, government expenditure, population age and others. The results of their scientific work showed that insurance is influenced by cultural predispositions toward uncertainty avoidance and by effects of regulation. Wanat, Papiėz and Smiech (2016) considered that this is the first paper which studied causal relations between the development of the insurance market and economic growth.

Webb, Grace and Skipper (2002) studied the influence of banks and insurance sector on economic growth. Their findings indicate that financial intermediation is significant. The authors demonstrated that penetration of insurance and banks is a staunch predictor of productivity growth. Moreover, they established that there is no causal network between economic growth and non-life insurance.

Kugler and Ofoghi (2005) found a causal link between the dimension of insurance market and economic growth in Great Britain over the 1966 to 2003 period. For estimation was used the Johansen test, but the authors doesn't include additional variables as Ward and Zurbruegg (2000) did. The results showed the connection between economic growth and different types of insurance, as life, non-life, motor and property insurance.

Haiss and Sumegi (2008) analyzed the impact of insurance on economic growth across 29 European countries, for the period from 1992 to 2005. They found that GDP in current prices per capita depends, among others, on written gross premiums, physical capital stock per employee and human capital stock, interest in the securities markets and inflation. They identified risk transfer and investment as major channels through which the insurance sector may aid in economic growth. They also take into evidence the impact of socio-demographic and legal issues and shows that these matter for insurance companies and for their influence to economy.

Arena (2008) has demonstrated in his study that both life and nonlife insurance sector has a significant and positive impact on GDP growth. He also identified that there are several factors that have influence on insurance, namely openness, inflation, government consumption, human capital, terms of trade change. The impact of private credits and stock market turnover, taken into account on study, was not demonstrated.

Feyen, Lester and Rocha (2011) shows that life sector premiums are driven by per capita income, population size and density, demographic structure, income distribution, the size of the public pension system, state ownership of insurance companies, the availability of private credit, and religion. They also show that the development of the insurance sector can be influenced by policy factors.

Chien-Chiang Lee, et al. (2013) provided a new study on relationship between insurance activity and economic growth. They took into account premiums, market share, rank, insurance density and penetration on GDP. The study indicated that a 1% increase in the real life premium raises real GDP by 0.06%. As a result, the authors have found that long-term development policies and liberalization of the financial sector could provide a development of insurance sector an overall economy.

The empirical studies take into evidence that there is a connection between economic growth and insurance sector. For long-time period this impact is positive and shows a contribution of insurance market on GDP level. Unfortunately, it is more about developed countries, while for emerging economies this impact is not significant. Nevertheless, there are some studies that demonstrate the existence of interdependence between economic growth and insurance in emerging countries, and this impact is positive, too.

3. The role of Insurance

The importance of insurance for an economy has already been demonstrated by the authors mentioned above. However it requires a more detailed analysis of this influence to highlight areas that need to be influenced to achieve a long-term development.

The role of insurance can be investigated in several ways. First, *economically*, insurance involving the accumulation of financial funds based on personal contribution of population through insurance premiums. The formation, distribution and usage of insurance funds involve socio-economic relations between the insured and insurer based on cash flows. The economic content of insurance relations is determined by economic laws and socio-economic rules.

In *financial* terms insurance is a financial intermediary between insured who creates funds and those who receive compensation in the case of risk happening. By insurance, people's savings arrive to financial market as investments also through insurance companies.

In determining of the insurance role we can not avoid the hierarchy of human needs presented by Abraham Maslow in 1954 where safety needs as security of body, family, resources and others are situated at the bottom of pyramid. It means that insurance is a basic need for all individuals that is based on psychology. So, *psychologically*, insurance aims to provide safety and psychological comfort as a result of risk transfer to insurer.

Essentially, insurance is considered a branch of service, a financial intermediary and a financial asset in an economy of uncertainty with effects on the whole economy. We can say that insurance have a contribution to the development of the national economy by maintaining the continuity of the production process, by protecting and defending the integrity of public, cooperative and private property, and by creating for the population of additional means for prevention, compensation and saving. Also, insurance has an important role in increasing benefits and participate in the process of gross domestic products distribution between economic sectors, territorial units and between business and population groups.

Besides financial, economic and psychological role, insurance also have an *educational* role. According to the contracts policy holders are encouraged and forced to take the most effective measures for keeping safety their properties which were taken into insurance. They are also forced to show an appropriate behavior towards other people being responsible under contracts of liability insurance. In case of personal insurance, policy holders are educated to take care of themselves.

Insurance has a significant *social* role. Their importance for social life is manifested by jobs creation; reducing economic uncertainties; making possible the resumption and continuation of normal socio-economic activity and giving the possibility to saving and fructifying of personal funds (through life insurance).

4. Determinant factors of insurance development

Theoretical and empirical studies have shown that the influence of insurance on the economy is determined by a several factors, named variables by Feyen, Lester and Rocha (2011) and grouped in 4 categories:

1) economic variables, including: inflation, income (income inequality) and the real interest rate;
2) institutional and market variables: financial development, state security share, foreign insurers share, market concentration, the legal framework;
3) demographic variables: population density, population, life expectancy.
4) social variables: education, religion, social security.

The authors Haiss and Sumegi (2008) positioned insurance in a similar economic environment as Feyen, Lester and Rocha (2011) did, but first authors have grouped them differently. In this case, religion, culture, risk propensity and age profile are grouped into demographic and social setting. The regulatory framework is viewed as a separate group with influences on the sector, as well as market structure.

We consider that the factors listed in existing empirical studies undoubtedly have repercussions on the insurance sector. Their influence is not always positive. For example, inflation, muslim religion, share of state insurance and market concentration has an negative impact on private insurance. However, we believe that the greatest consequences on the insurance development have the regulatory framework changes, population culture (including financial culture), demographic structure and revenues.

In existing studies we did not find the *geographical factors* as variables that have an influence on insurance. We think that they are particularly important, because their impact is significant and determines the profiles of insurance companies. For example, in areas with high probability of typhoons or floods are very developed the property and life insurance. In countries with well-developed financial markets, the most diversified insurance packages related to financial risks.

As well, we propose to delimitate the *political factors* that has a significant influence on insurance development. For example, the entry ban for refugees and migrants introduced by US President Donald Trump in January 2017 affected the travel and health insurance sector of European companies, especially in the UK.

5. The influence of insurance on economic growth

From the literature review, we found that insurance effects on economic growth have been less studied until present. The most extensive studies refer to the connection of banking sector and stock market with economic growth. The studies were promoted by King and Levine (1993a, 1993b) and Rousseau and Wachtel (1998). Nevertheless, there are a few studies about the influence of the insurance sector on economic growth. Among them we can mention the work of Ward and Zurbrueg (2000), Kugler and Ofoghi (2005), Marco Arena (2006), Haiss and Sümegi (2008), Pei-Fen Chen et al (2009), Chien-Chiang Lee et (2013), Botnari and Teaca (2010), Kjosevski (2011).

Most often it is considered that the insurance market is focused on two directions, on the one hand it is financial intermediation, and on the other - the risk transfer and compensation (Haiss and Sümegi, 2008). Thus, insurance contributes to economic growth through more efficient management of various risks, which encourages the accumulation of new capital, but also by mobilizing domestic savings (household savings) into productive investments.

In 1997 Harold Skipper said that the insurance business, in addition to risks covering, has the function of institutional investor and contribute to economic growth. The ways in which insurance contributes to society and economic growth can be summed up as follows:

a) it increases the financial stability of families and businesses;
b) it facilitates competitiveness and trade development (the oldest occupation of insurers);
c) it contributes to increasing solvency, reducing the capital cost and decreasing risk what motivates entrepreneurs to start new businesses and to assume additional risks;
d) it mobilizes domestic savings;
e) it allows different risks to be managed more efficiently;
f) it helps to relieve the burden on governments for providing all services of social protection to citizens via social security systems;
g) it fosters a more efficient allocation of capitals;
h) it contributes to loss mitigation;
i) it facilitates the long term investments (in case of life insurance).
j) it promotes solvency.

To highlight the role of insurance in an economic system and their contribution to economic development we will present their financial circuit (Figure no. 1).

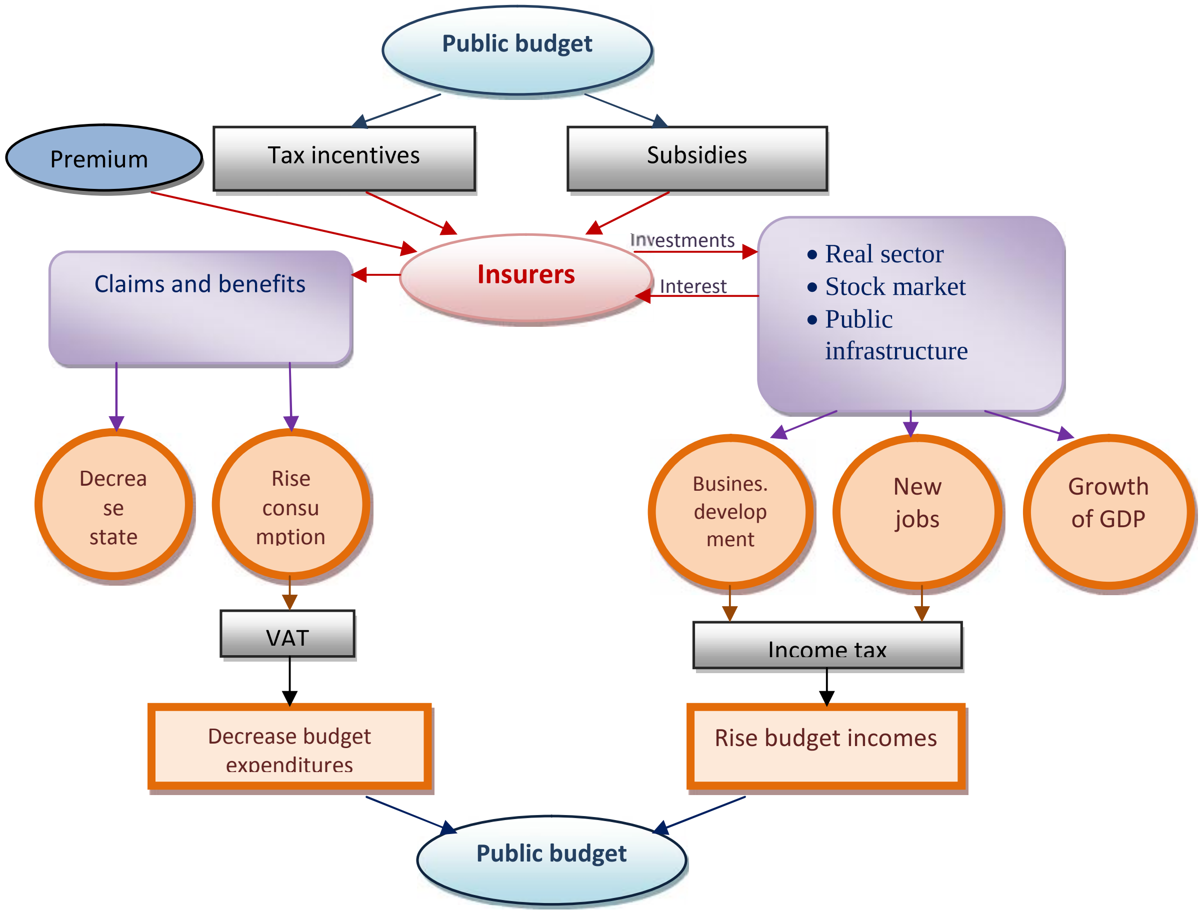

Figure no. 1. The role of insurance in an economy

Insurers, especially life insurance companies, create their funds by government investments, marked by tax incentives and subsidies, and by population investments marked by paid premiums. From these funds, insurers paid compensation and benefits that actually represents savings and retirement of population. Similarly, from these funds they make investments in the financial market, real sector and state infrastructure. This helps to develop the production process, the financial sector and the economy in general, what promote a GDP growth. This mechanism demonstrates the contribution of insurance to the economic growth. There is also a cyclical movement that shows the reverse contribution, namely the contribution of economic growth on insurance. Thus, economic development entails the creation of new jobs, increasing consumption and rising turnover and profit of enterprises. All these effects contribute to increasing the volume of collected taxes on VAT, individual income and corporate income. Together with the reducing of the state burden promoted by insurance, we arrive to the idea that, on the one hand, insurers increase state revenues; on the other hand, they reduce their expenditures and strengthen public budget by this way. From here we distinguish that a strengthened state budget can contribute to the stimulation of the insurance companies. This cyclicality demonstrates that insurance industry and socio-economic process in a country are interdependence.

6. Conclusions

The results of our studies show that insurance is an important economic category. Due to funds made up of paid premiums, insurers are important players on the investment market. Lending and long-term financing capabilities contributes to business development or to the economy development overall. Insurance is the main generator of certainty in the business and in the family life. By specific cash flows and through their distribution according to the principle of mutuality, insurance promote the continuity of the production process. Reinsurance operations on the international insurance market have a contribution to the expansion of international trade relations, but also have an influence to the balance of payments.

Therefore, insurance contributes to economic development by protecting and defending the public and private integrity, by ensuring continuity of production processes, but also by supplying the long-term financial resources.

At the same time, insurance has a major socio-economic importance due to the job creation, contribution to enhancing added value, people education in terms of assets protection and providing of psychological comfort and tranquility.

The insurance sector in turn is dependent on the economic, demographic, political, institutional and geographical factors. These interdependencies of insurance with other sectors show that there is a cyclical circuit of cash flows involving insurance. We consider that this mechanism is more functional in development economic systems.

The research has highlighted the fact that there is a link between economic growth and insurance sector. For long term, this impact is positive and is determined by the contribution of the insurance market on GDP growth and thus on strengthening public budget.

The results can be used by governments to achieve the intended level of economic and social performance. By stimulating the insurance business they can contribute to the economic growth. Thereby, the government influence through the factors described in the paper could contribute to the development of the insurance sectors and by the domino effect could lead to the economic development.

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