Global Advanced Research Journal of Economics, Accounting and Finance (ISSN: 2315-5124) Vol. 5(1) pp. 001-007, December, 2017
Available online http://garj.org/garjeaf/home

Full Length Research Paper

Impact of the Financial World Crisis on the Arabic Insurance Market

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Accepted 24 November 2017

The economic effects of the current financial world's crisis included acute declines in economic output, a decline in the value of currencies, and rises in inflation, interest rates and aggravated debt, all that produced multiple effects on the Arab and world insurance market, presented in the declination of demand for insurance, which led to a decline in new business , rise in insurance rates , caused an increase in the value of claims as a result of price increases and existence of mismatch between assets and liabilities, which reduces the solvency of insurance companies.

Keywords: world Financial Crisis, insurance ,Takaful Insurance.

INTRODUCTION

The world financial crisis began in 2007, but what is characterized it rather than the crisis in 1929, that the declination became globally, and included all the financial and banking services, which intersected with each other as a result of globalization of markets.

Research Problem

The nature of the insurance companies business differ from banks because they do not create credit or liquidity, but they absorb liquidity in the community as well as government subsidies to insurance companies is not available in the economic activity, so the economic effects of crisis of the financial world on the banks differ from insurance companies although there is a similarity between the banks and insurance companies. The problem of the study tried to answer the main questions: What is the impact of the global financial crisis on the Arabic insurance sector?

The importance of research

To focus on the risk arising from the bankruptcy of the banks and reduce the risks arising from the bankruptcy of insurance companies during the financial world crisis.

Banks engage insurance business in what is known insurance banking. This means risk transferred from banks to insurance companies.

Some countries have tended toward unifying control of their insurance companies in one umbrella.

Research objectives

To identify the reality of the insurance industry in the Arab world.
The effect of the financial world crisis on the Arabic and the world insurance market.
To identify the new mechanisms of the insurance companies and the measures needed to address this crisis.

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RESEARCH METHDOLOGY

The study relied on the analytical descriptive approach To diagnose the causes of the global financial crisis and its impact on the Arabic conventional and islamic insurance market

Causes of The World Financial Crisis

Growth of the Housing Bubble

American Federation Corporation Guarantees for insurance decline of the rate of interest on the loans of families' deposits who have limited income until it reaches (1%) (Ahmed, 2008) to provide liquidity, where it lead to refresh the market and rise up the real estate sectors procurement, to increase the prices, so the banks in United State grant loans to thousands families whose income is limited without any efficient guarantees with high risks against high rate of interest depending on the high rise of price of housing, so as to get great profits (Yasir, 2009).

Rises of Real-Estates Price and Rate of Interest

The price of real-estate specially housing witnessed high price during the period (1997-2006) until it reached about (124%), which pushed most of them to lend in order to finance purchasing their own houses , where the rate of property's housing in United State of America rises from (64%) in 1996, up to (69.2%) in 2004.

Most of the owners lend with its value, which is not paid yet, the price, Home prices were pushed up by increased demand for housing. The value of the building increased with continuing the guarantee. In 2006 and 2007, the rate of interest gets unexpected rise, leads to weaken the commitments of the limited income, and increase the housing bubble which they get and commit to build and purchase it, and the loans which granted due to the guarantee of the building itself, that reduce their ability to pay, so they became unable to pay the high installments of the loan which they lend, so this push the bank to pay the citizens' debt in a form of securities to the international investor, were they insured it, and after the crisis rises the bank and insurance companies are bankrupted.

Excess of derivative credit, or credit risk exchange tools.

When the bank lends someone, the bank will be serious to take enough guarantees to pay, because if the lender bankrupted, the bank would loss. But if the bank took guarantees of the loan, the bank would transfer the risk of the debt to the third party, in this case, the bank will not lose, if the lender is bankrupted, because the third party will commit to pay the value of the loan completely in this case. So the bank has not enough incentive to insure the solvency of the lender. So the banks do not face any difficulties to lend the subprime person because others bear the risk, which are almost insurance companies and hedging fund. This insurance on loans encourages banks to lend, and then sell loan on the form of securities, with insurance to these securities. Who buy these securities that means he buy debts insurer, it does not matter of the subprime of the lender or his creditworthiness, but what are the interests of insurance companies and hedging funds to insurance on these loans?

First: cash fees to get them, which is attractive fee if a portfolio is large the managers incentives depends on the amount of earned income, and therefore the higher the fees increased incentives. Second: as long as the property or assets that are financed at higher prices, there will be no risk of faltering, because the borrower can restore the property fund a new loan, or it can be to pay off the debt and obtain additional profit selling the property.

Third: the insured risk can sell to others, either singly or in a vehicle with other risks, in the form of bonds mimic the same loan bonds, it gets for it an extra fee. The buyer of these bonds could in turn sell them, and then it lessen risk to others. Market members are still scrambling risk aversion among themselves; all hoped that the ball will not explode in his hand. Whenever the market is the largest and the players in it, the more the probability of risk aversion explosion, however, one of them is less, so the acceptance of the biggest risks. That is why the market was inflated in the interest of adventurers, and this explains the doubling of credit risk market more than eight times during 2004-2007 until it reached 62 trillion dollars (Steve, 2008)

World Insurance Market and Takaful Insurance and Bank Assurance

World Insurance Market and Takaful Insurance (Publication of Swiss, 2009)

In 2007, According to the studies engaged by Swiss Re Reinsurance company, which stated that the world insurance premiums reached 4,061 billion dollars *(2,393* USD life insurance and general insurance non-life 1.668 billion dollars) the percentage increased in 2006 to 3.3% and 5.5 for life and (0.7%) non-life insurance. The largest share of this amount is for industrialized countries, accounting for 90% of the total premiums or 3644 billion (an increase of 2006 by 2.4%) The decline in the growth rate of premiums of life in industrialized countries at a rate of 5.3% did not transfer to positive rate compared to 14.5% for the developed countries due to variety in premiums volume. It was clear that life Insurance in industrialized countries were most affected by the financial crisis and economic downturn, this is normal and commensurate with the quality of the insurance policy linked with unit linked returns and insurance policy with a single premium, so the negative impact of markets became large, where these documents are prevalent such as the UK, France and Ireland.

Despite the decline in premiums, the results underwriting were satisfactory and profits close to the results of underwriting in previous years, but the loss of investment funds, insurance companies were big, the insurance industry were recorded decline in the share capital between 15 to 20% for the general insurance and 30 to 40% in life Insurance.

Average spending Insurance in industrialized nations arrived in 2007 to U.S. $ 3,577 per person (U.S. $ 2,143 for life insurance of $ 1,434 and General Insurance) was 270 dollars in 2006 per person. Higher average spending per person was in Ireland about 7,000 U.S. dollars, followed by the United Kingdom.

Taiwan comes in first place for the share of the insurance to the GDP, where it reached in 2007, higher than 15%.

Premiums of developing countries in 2007 were 414 billion dollars equivalent to 10% of the total premiums of the world. The average spending per person was $ 72 (about $ 53 for the year 2006) Total spending reached for the life insurance $ 38 and $ 34 for non-life insurance).

The premiums of Middle East and Central Asia reached 23 billion dollars equivalent to *0.5* 7% of the total world premiums and an average spending was $ 75 per person.

Still world insurance companies owned more than 80 percent of the reinsurance premiums because of the large capital and its long history that extended to more than 130 years in the insurance industry.

Experts of the insurance industry around the world agreed that the climate change, globalization and terrorism were the most challenges facing the insurance industry, which neither banks nor for companies became the main base for world trade, and without it cannot be able to conduct their work.

The volume of transactions in the insurance industry, including mergers and acquisitions 6. 23 billion dollars.

United Arab Emirates, is the largest insurance market in the Middle East, has experienced nominal growth in 2006 of 27%, where the total value of premiums are 7.2 billion dollars. In the meantime, do not exceed the share of insurance services of the GDP of the Gulf region 7.1% compared with globally 5.7%.

Takaful Insurance (World Union in Takaful Insurance Companies)

The first Takaful insurance company in Sudan founded in 1979 and then the idea of Islamic insurance spread after that particularly in the past five years, and now the number of 'Takaful insurance companies is about 250 companies (IMF. Regional Economic Outlook, 2009).

The subscription of the Takaful companies in 2006 was about 2 billion dollars, one billion in Gulf countries is (Iran included to this number, the Islamic insurance reaches 5.6 billion dollar), but it is very fast growth, where in Gulf countries the growth reaches more than 40% annually, according to Standards and Poor's Co. study, With the opening of the Saudi Arabian market for Takaful insurance, it is expected that subscriptions in the Gulf countries will reach up to $ 4 billion in the coming years, according to studies.

Saudi Arabia is now the large Takaful insurance company, where in 2006, the subscription reaches about 831 million dollars, and the second solidarity insurance is Malaysia where subscription reaches approx 530 million dollars.

The rate of growth of the Takaful sector exceeds the growth rates of traditional insurance one, at the time that the annual growth rate for premiums of the world insurance is 2.5% and the Takaful market in the Middle East is growing at a rate of 20% per annual (Newsweek magazine, 2009).

The phenomenon of a shift towards Takaful insurance in the West has grown, so (AIG) American company founded Takaful insurance in Bahrain and then followed by (RE- SWISS) Co.

Bank Assurance

The experiment began in Europe and for decades Spain and the UK banks sell insurance products but in America the law (GLss Sreagall) prevents banks from entering the insurance market until 1990. But France was selling more than (70%) of insurance products through banks the banking insurance in Europe Represents proportion (50% -90%) of the Life insurance, but life insurance is few in the Arab countries, and it is started with limited experience in imposed formula accompanied with banking products such as mortgage insurance in Morocco and Kuwait (Nalini, 2007).

American Insurance Market

The effect of 1999 act on insurance industry in U.S.A (George, 2006)

The new law has main effect on organizing insurance at the level of America, these possible effect includes:

Increase competence between insurers, banks and other financial institutions.

Organized the insurance divisions in the state to buy insurance through companies instead of insurance companies as banks which did not compel to full control on specific areas such as the financial subprime.

Merges and properties of the insurers other financial institutions can be invested.

Small insurer can be more probably controlled by the large insurers.

Some financial institutions try to linked financial product sales with insurance sales which can harm consumers.

There is a needs to coordinated and cooperated between the different organizers of the financial institutions.

The financial insolvency of American insurance companies and the story of the largest American company (AIG) that had gone bankrupt (George, 2006)

Financial insolvency problem insurers remain the task of organizing the problem. Between 1991- 1998, there were 805 insured companies were liquidized, during the same period there were 344 reformed (AIG) is one of the largest companies in the world, sales of a total of $ 113 billion in 2006, a number is now used more than 116 thousand employees in 130 countries extending across the continents .

(AIG) in the fourth quarter of 2008 have suffered a net loss of $ 60 billion.

The causes of the financial collapse of American insurance companies (Journal Pioneer, 2008).

Lack of compensation needs:

During 1969 to 2002, The reason of the shortage of reserve compensation (37.2%) of the situation of financial deficit to the insurance companies. This ration was between 1991-2002 about 48.6%, this increase is due to the large increase in claims to compensate those infected of pollution caused by Esposito.

The Rapid Growth of Deficits Was Due to Fraud

The rapid growth (17.3%) caused deficit in insurance sector between 1991-2002 and before this date the rate is more than (11.7%).

In case of the financial deficit which caused by shortage in compensation reserve, or rapid growth, but price is not included in the main reasons which contributed to financial deficit.

Lack of Guarantees and Insurance on the Securities That Have Bad Financial Assessment

The global financial system requires that securities (financial assessment) , who owned bad assessment, It has a bad rating, resort to pay a fee to the insurance companies that undertake to pay the value of the bond if the bank fails to repay the value of the asset or the demise of the guarantor of the bond.

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Failure to regulate the commercial types

Disorganizing the commercial types for large commercial accounts. Legislation which excludes insurer from amend the prices and form of documents, and the large commercial accounts with insurance department to the state to approved it.

U.S. financial procedures for the Treatment of the financial crisis for banks and insurance companies (Waleed, 2008)

The U.S. administration carried through banking rescue plan which added a little amendment and approved by Congress in 2/ October/2008, to address the crisis, where this plan let the state to buy the depreciated assets linked to the mortgage value of 700 billion dollars to:

The state Contribute in the capital and profits of companies benefiting (nationalization).

The minister of treasury charges to create Control Council and the General Accounting Office and general independent inspector.

Coordinate with other countries to take similar action.

Raise the guarantees target to depositors from 100,000 to $ 250,000 dollars for a period of one year.

Granting tax exemptions valued at (100) billion dollars for the middle class and companies

Determine the financial rights of the heads of companies who are dispensing with their service.

Federal Deposit Insurance adopted new regulations pave the way for private equity institutions to buy U.S. banks that failed to meet standards set by the institution.

Arab Insurance Market

Characteristics of the Arab insurance market

The small size of most companies does not help to increase the retention of risks and operate these companies as brokers, in some cases. The retention ratio of the total Arab market in motor insurance is about 40% of the total premiums, noticing that the large part of premiums related to the risk of amount its insures is small. It can increase the retention ratio to higher rates. (Journal Pioneer, 2008).

From the available statistics were estimated rate of capital in an insurance company in the Arab world is amount of thirteen and a half million dollars per company and the rate of gross premiums per company, in that Arab world, which amounts to about 14 million dollars. The rate is one to one only, enhance clearly the idea of million dollar exists are frozen in the capital of the small companies that have low income, where we request for foreign investment in most of the Arab countries. (Journal Pioneer, 2008).

National insurance companies currently subscribe (100%) of the business in most Arab countries, in addition to most of the foreign on behalf in the market that belong to foreign economic activities in their countries (Journal Pioneer, 2008).

The volume of premiums written in Arabic insurance market is (15) billion dollars, and this is equal to 1% of GDP for the Arab States, according to the statistics of 2007.

The complete openness countries (GCC) achieved the highest percentage *(54.6%)* of the premiums in an insurance Arabic market. The middle or above openness countries achieved rate (36%) of it, But the third group countries, the low openness countries achieved (9.4%). (Journal Pioneer, 2008).

Life Insurance's share of the total premium does not exceed *(15%)* compared against more than *50%* in the insurance markets of the industrialized countries.

Insurance density of the Arab insurance market: is relatively high in the countries of the Gulf Cooperation Council, come first in comparison with the rest of the Arab markets. This is due to the special combination of the economics of this region, in terms of large-scale projects of the infrastructure on the one hand and the relatively low population and high rates of income of individuals on the other hand.

Although the level of income of individuals in a number of GCC fluctuated with the level of income of individuals in developed countries, the contribution of individual GCC countries in the size of the income from premiums much lower than the industrial nations and contribution per capita is (1000) U.S. $, compared with one-third of the rate in the Arab contribution in this area (IMF. Regional Economic Outlook, 2009).

The Weakness of Capitals

Except of limited number, the majority of the Arab Insurance companies suffer from the weakness of their capital compared with companies in developed countries. less than (10%) of the capital of Arab insurers exceeds 100 million U.S. dollars.

The weakness and decline of the capital in the Arab insurance sector is due to:

Inadequate interest and believe of investors in this sector.

A number of insurance companies are possessed by the families or local business houses do not accept to enter into partnership with others in the ownership of these companies (Newsweek magazine, 2009).

The size of the Arab insurance companies retention about 62% of total premiums compared with the percentage of retention (80%) of similar companies in the advanced industrial counters now, the most capital of Arab insurance companies is relatively low retention is.

The traditional arrangement for reinsurance remains governed the relative agreement and optional reinsurance as a model of participant and production between direct insurance companies and reinsurance companies, a number of Arab countries depending on the international market for reinsurance is still high, especially in markets that have significant risks, such as the risk of oil and petrochemicals (IMF. Regional Economic Outlook, 2009).

Currently, there are three Arab insurance companies classified in category (A) by the standard and poor's, (23) companies which has been assessment from (367) Arab insurance company. This is an addition to (18) companies in the category (BBB), and two are less than that, theoretically (IMF. Regional Economic Outlook, 2009).

The effect of Crisis on the Economics of the Arab Countries

The economics of the Arab countries definitely will affect by the world financial crisis, because this crisis affected the world economic all included the Arab economic.

The crisis created economic stagnancy for (30) states of United State of America and threaten (19) other states, also affect the Euro economics in stagnancy and the Japanese economics, this stagnancy is affected the economics which consumed energy in the world , so it lead to reduce consumption and effect the price of the primary materials (Waleed Ahmed, 2008).

The positive effect of the World financial Crisis on Economic and World and Arabic insurance Markets (Newsweek magazine, 2009)

The decline consumption and purchase fever caused by senseless of ease to the economic situation and its future, this causes reduction of company and factory's products on demand**.** The Consumer used their mind carefully to purchase what they need only.

Migration of industries in search of insurance and health care markets, operated in low cost and as an example: U.S. auto factories transferred much of its production to Canada to take advantage of the low costs of health care since 2004.

Negative economic impacts of the World financial crisis on the economies and World and Arabic insurance markets(Newsweek magazine, 2009)

The role of government reduced to establishment a social safety network, and the citizen must pay cost related to the health care, so when they retired they cause saving.

Some countries' population get elders for example Japanese and their Retirees expense their saving in high pace. Some countries as America prefer to expense on savings, because all programs and incentives to enhance people to expense is still valid, where United State is the unique country that do not request national tax on procurements.

The rising cost of health insurance, where each (10,000) of Americans are losing their health insurance every day, in 1993 there is (61%) of small businesses provide health insurance to their employees, but that percentage dropped to 38% during the global financial crisis.

Increasing savings rates due to the disintegration of the social safety the government companies provide their employees health benefits and pensions, but these benefits are stopped and forced workers to save more money in anticipation of the disease and aging.

The collapse of banks affects the insurance companies, which owns some of the capital of these banks. For example, gint frech company have the greatest loss occurred when the collapse of the Lehman Brothers bank, because it owns (20%) of the capital. Insurance companies generate interests from subscriptions and investment after world and local financial market has been declined, which leads to decrease the rate of investments interests, the bankruptcy of insurance companies means lack an important tool in directing savings toward investments.

Some Arabic insurance markets have been affected by what happened for (AIG) Company, such as Saudi Arabia, the company insured in the Saudi market (3%) , also the company contribute in insurance on energy sector by *5%.*

After the world financial crisis the reinsurance companies intensive with its conditions and prices during renewal of reinsurance treaties.

The size of the insurance market declined as a result of the Arab GDP declining and decreasing of Exports and imports, thus affecting the marine insurance and export insurance. The contribution of the Arab countries in global economic growth reduced (2.5%), except of oil, this reduced the direct impact of the global crisis although the decline of oil price did not affect the Arabic Petroleum countries because of oil redundant during the previous period, but affect the countries who invest in housing, increase the claims caused by morale risk.

The decline of insurance company shares prices. The rising cost of reinsurance in the Arab countries because of the Low commissions **b**acking into agreements relative returns. Raise limits retained when the renewal agreement exceeded the loss, national reinsurance companies may raise their prices like the corporate world.

World financial Crisis effect on Arab Takaful Companies(crisis in Arab countries)

The Takaful insurance companies are part of insurance globalization effected by the world financial crisis as the following;

It depends on the world price of reinsurance.

Investment Income and profit decrease affected in:

The rate of insurance redundant which distributed between policy holders and shareholders and Islamic Insurance companies are differ, because Islamic Insurance Saudi companies distributed the surplus insurance (10%) for the policy holders and 90% for shareholders.

Insurance do not give flexibility in insurance price and them premiums will cheep.

The Islamic Takaful experience is new and are limited, this gives high flexibility in facing the financial crisis, because it used tools of Islamic finance and provides services for those who advocate Islamic experiment.

CONCLUSIONS

After the world financial crisis, the insurance companies focused on their main activities to raise the revenue from the operation, after raising the insurance price and auditing the quality of insurance covering before the administration of insurance reduce the probable losses, the insurance companies before the world financial crisis depend on collecting profits from investment on stock market and financial participation.

The demand is decreased with dropping the rate of interest. This reflects on the insurance activity and show the need to reprised a number of insurance companies.

Immigration of the world insurance companies to counties that have less cost of insurance, this may change the map of insurance in the world and the Arab countries.

More insurance companies are affected by the world financial crisis, which is associated with the banks, contribute to transferring the bank's risk to the insurance companies, especially the insurance companies that invest in bank deposits and market's capital.

Contradiction between the roles of central banks as a lender to banks and between the insurance which depend on the bank deposit.

The Arab insurance companies affected by the world financial crisis because they depend on the world price of reinsurance and the degree of premiums retention.

RECOMMENDATIONS

Establishment of a subsidize fund to insolvent insurance companies that unable to pay claims for compensation similar to what happens in New York state, which all insurance companies contributes in this fund.

Allow shareholders to be funded by other insurance companies after confirming that it is better than the first insurer company.

Provide interactive insurance control, and held a training programs to strengthen the supervision and control devices.

Engage researches helped in decreasing the insurance's price through reducing commissions and expenses and make awareness to insurer how to protect and prevent what leads to decrease the rate of losses and then the payment premiums.

Encourage researchers to provide applied research from an Arab perspective to create new insurance services. Support Arabic cooperation in the field of insurance and reinsurance and cooperate with Arab experts of insurance to address Arabic strategies in the field of insurance and reinsurance to face the world challenges and internal glomeration.

Establish Arabic bank for insurance information covers to all technical and financial aspects of the Arabic insurance sector.

Review the policies and controls of granting credits and strength on it, without taking consideration of the policy or social or any other things.

Form a committee to attract money escape by crisis and directed it to the agricultural and industrial product sectors , specially Arab financial which began to escape from the United State to more security places.

Reconsidering the insurance funds on Arabic deposits and to understand the different nature of banks and institutions, and take into account exist of one control departments for both banks and insurance companies.

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