AN EVALUATION OF THE IMPACT OF THE CONSOLIDATION OF THE INSURANCE COMPANIES ON THE ECONOMIC GROWTH AND DEVELOPMENT IN NIGERIA.

BY

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M.SC/SOC-SCIE/06221/2006-2007

BEING A RESEARCH THESIS SUBMITTED TO THE DEPARTMENT OF

ECONOMICS FACULTY OF SOCIAL SCIENCES AHMADU BELLO UNIVERSITY, ZARIA.

IN PARTIAL FULFILMENT OF THE REQUIREMENT

FOR THE AWARD OF MASTERS DEGREE IN ECONOMICS

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JUNE 2011

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AUGUST 2011

DECLARATION

I declare that the research work on the topic "AN EVALUATION OF THE IMPACT OF THE CONSOLIDATION OF THE INSURANCE COMPANIES ON THE ECONOMIC GROWTH AND DEVELOPMENT IN NIGERIA" was carried out by me under the guide of my supervisors.

The information provided in this work has been properly referenced and acknowledged. No part of this thesis has been presented as it is for any degree or diploma programme in the same area in any University to the best of my knowledge.

Yusuf Mohammad Awwal …… ……

Signature Date.

CERTIFICATION

The thesis on "AN EVALUATION OF THE IMPACT OF THE CONSOLIDATION OF THE INSURANCE COMPANIES ON THE ECONOMIC GROWTH AND DEVELOPMENT IN NIGERIA meets the regulation governing the award of Masters of Science (M.Sc) Degree in Economics by Ahmadu Bello University Zaria and is hereby approved for it's contribution to knowledge and literary presentation.

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DEDICATION

Dedicated to my Alhaji Angulu Musa Shuaibu and Hajiya Hawwa Abdulkareem (Parent)

Dedicated to Abdurrahman Yusuf (Late son)

ACKNOWLEDGEMENT.

All praises is due to Allah for His infinite mercy that made this programme come to an end successfully.

The programme was carried out with ease due to support many people rendered to me directly and indirectly. I am very much grateful to my supervisors Dr Ishaya and Professor .(Mrs) P.S Aku for painfully going through the work and making constructive suggestions for progress. In the same vain I appreciate the support received from Professor Mike Kwanashie, Professor A.Garba ,Dr Njiforty , Dr Sanusi Rafindadi and all members of staff of the department.I am greatly indebted to my parents Alh Angulu Musa Shuaibu and Hajiya Hawwa Abdulkareem and my uncle Mallam Mohammad. My lovely wife Mallama Salamatu and children Mohammad Habibullah, AbdulHafiz, Hawwa (Ummi),Sumayya,Munirah and Abdussalam for their understanding, patient, and all their support in the course of this programme. I really appreciate you all.

The list will be incomplete without the names of Alh sule Yusuf and family,(Executive Director,Best Homes Abuja), Alhaji Abdurrahim Sulaiman (Director of IET Abuja) and Alhaji Usman Mohammad (Senior Brother) and family, Sheikh Ahmad Jarma ,Late Alhaji Yusuf Ladan Barnawa and family for all their over whelming support.

The thesis of this type could not be achieved without the support from my professional colleagues and friends such as: Simon Ojonye (Neoclassical),Mashin Mohammad,Adam

Shuaibu(Abu-Abdurrahman), Danraka N. Dari (Baba bee) and family, Alh Yakub Annivasa and family, Mal Salih Ibrahim Kyagama and family and all my class mates.

My younger ones have done their own part towards my success.They are:Usman (junior brother),Omehi Keke,Maimuna,Nndagi,Ibrahim, Ayisha,Sani,Amina ,and Aliyu.Also Ibrahim(Dantala),Habiba,Abdullah(Daddy),Nafisah,Bilkis(Iye) and Abubakar.My senior sisters Onja Aibetu,Onja Mama, Onja Babu and others.Thank you for all your support.

My In-laws Mallam Abdulkadri and Mallama Sifau ,Amina (Turayo),Zainab, Lawal(Lanre) ,Abubakar (Tunde) Rahmatu, and Jamiu I remain very much grateful for your unending support and understanding.

ABREVIATIONS.

CBN :Central Bank of Nigeria

GDP:Gross Domestic Product

NAICOM:National Insurance Commission

IBER:Insurance Business Environment

SPSS:Statiscal Packages for Social Sciences

NBS:National Bureau for Statistics

FSS: Financial System Strategy

ABSTRACT.

The research carried out is on Evaluation of the impact of the consolidation of insurance companies on Economic growth and development in Nigeria. The main objective is to evaluate the impact of the Insurance Companies' consolidation on the Gross Domestic Product (GDP) in Nigeria. The Econometric technique method of analysis was used. The econometric model was based on Capital Assets Pricing Model (CAPM). Relying on data collected an in depth analysis from 1988 to 2008 shows that the Gross Domestic Product (GDP) of the economy would increase by about 55 percent variation for a unit change in the consolidation policy while holding other economic variables constant. This scenario leads credence to the fact that consolidation policy has positive impact on the economic growth and development of the country if all structural bottlenecks to implementation are removed. It is also recognized that the impact of consolidation policy on insurance companies to achieve the desired economic growth and development may not be necessary contemporaneous, but long lived if properly managed-especially as capital projects and human activities tends to have long gestation periods. To achieve intermediate and long-term economic aspirations to make Nigeria among the 20th most industrialized countries of the world (FSS 2020), efforts should be directed to develop a modern, well-structured, efficient and competitive insurance sub sector that caters for the long term needs of the economy.

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CHAPTER ONE

GENERAL INTRODUCTION

1.1 BACKGROUND OF THE STUDY

Many of the fundamental debates regarding the efficient operations of the insurance companies have been wide ranging but not so convincing. While such recorded arguments often posits that insurance companies provide services that are capable of generating productive resources such as increased profits, productivity and investments for the long term growth of the economy, the extent to which insurance companies offers to under write risks, facilitate innovations and develop productive initiatives through policies and coverage remain daunting.

Historically, Insurance business evolved simultaneously with the appearance of human society in which insurance businesses are practiced in the form of people helping each other. Earlier form of transferring or distributing risk (insurance) were practiced by Babylonian and Chinese traders in the 2nd and 3rd millennia BC respectively. Then, Chinese traders travelling treacherous river rapids would distribute their wares across many vessels to limit the loss due to any single vessels capsizing. In the Babylonian case, they developed a system which was recorded in the famous code of Hammurabi, c.1750BC and practiced by early Mediterranean sailing merchants.

However, the first recorded insurance cover was done by the Achaemenian monarchs of ancient Persia who insured their people and made it official by registering the insuring process in governmental monetary offices. The purpose of registering was that whenever the person presented a gift to the monarch, if at any time such a person is in trouble, the monarch through a specialized court will help him.

Equivalently, the Greeks and Romans introduced the origins of health and life insurance c.600AD when they organized guilds called" benevolent societies" which cared for families and paid funeral expenses of members upon death.

The most formalized insurance business was established in the late 17th century in England when people, through the "friendly societies" donated amount of money to a general sum that could be used for emergencies. Yet, the post-Renaissance Europe started a more sophisticated insurance business through which a specialized varieties of insurance were developed. Today, insurance business as it is well known can be traced to the great fire of London in 1666 which devoured more than 13,000 houses. The devastating effects of the fire converted the development of insurance "from a matter of convenience into one of urgency" a change of opinion reflected in sir Christopher Wren's inclusion of a site for insurance office in his new plan for London in 1667.This scenario led Nicholas Barbon and eleven associates to established England's first fire insurance company in 1681.Initially,5000 homes were insured by Barbon's insurance office. This development spread to other parts of the world. For instance, the first insurance company in the US under wrote fire insurance and was formed in Charles town(modern-day Charleston),South carolinia in 1732 through the help of Benyamim franklin who popularized and made standard the practice of insurance, particularly against fire in the form of perpetual insurance. In 1752,he founded the Philadelplia contribution ship for the insurance of houses from loss by fire.

Traditionally, some forms of social insurance schemes existed in some part of Nigerian societies. This simple form of social insurance was practiced by means of cash donations, organized collective labour of assisting one another and entire community who suffer mishap e.g illness, funeral, or important ceremonies.

In Nigeria, insurance business came with colonialization. The colonial authorities established the insurance company, which up till independence were dominated by oversea operators-with only three (3) out of twenty five(25) operating in the country. This was done to create a risk management instrument and product that are customized to the peculiarities of various areas of economic endeavour for overall economic activities that may not have taken place otherwise.

1.2 STATEMENT OF RESEARCH PROBLEM.

The Nigeria Insurance Companies was characterized by tUnder capitalization, dearth of human capital and professional skills, poor return on capitals, prominent of unethical practices ,non prompt payment of claims, low GDP per capital figures, lack of innovation in product development, lack of awareness on the part of the consumers on the uses/suitability of insurance products etc. These problems lead to the development in Nigeria whereby all existing properties at the Federal, State and Local government levels are less that 10% insured while household items have insignificant proportion of insurance with more than 70% of private property and businesses uninsured. These gaps in the underwriting of insurable risks for economic growth have remained wide up till today due to the failure of various consolidation policies of the government. These concerns underscore the need for this study. Therefore, this is expected to stimulate the minds of policy makers in the insurance industries, the need to formulate credible policies that will guarantee insurance underwritings for all Nigerians and their property.

Many of the researchers on the evaluation of the impact Insurance companies' consolidation to economic growth has provided a fertile interface between economic theorists and empirical economists. In most cases, conclusions from such studies attempt to link the risk management systems of the insurance industries through their risk taking abilities that are capable of eliciting innovation for the growth and development of an economy. This is achieved when insurance companies pools investible funds by offering risk management services relating to life, business and market activities for insurance premium.

It was the realization this that the Federal Government of Nigeria came up with the consolidation exercise in 2005 with the measure –"The Nigerian Insurance Market Development and Restructuring Initiatives(MDRI)" – aimed at addressing the issue of compulsory insurance products, insurance agency system, fake insurance institutions and risk based supervision. Therefore the study will attempt to find answers to the following questions:

(a) Has the consolidation of the Insurance companies improved the economic performance of the Country?

(b) How has insurance companies been creative/proactive in order to effectively carry out their businesses?

(c) What are some of the Post consolidation challenges facing Insurance companies in Nigeria?

(d) What policies that can be introduced or strengthened to ensure that insurance companies carry out their business satisfactorily?

1.3 OBJECTIVES OF THE STUDY

The main objective of this study is to evaluate the impact of Insurance companies' consolidation on the economic growth to the Nigerian Economy. The specific objectives are to examine:

(a) To Examine impact of consolidation of the Insurance companies to the GDP..

(b) To examine what post consolidation initiatives embarked on by the Insurance companies to improve their products and services delivery.

(c) To examine what are some of Post consolidation challenges facing Insurance companies in Nigeria.

(d) Make appropriate recommendations for improvement in performances of insurance companies based on the results of the study.

When these objectives are realized, the study will help to "inject" a fresh look at the activities undertaken by Insurance companies and thus reconcile all the apparent differences between consolidation policies and the vacuum created by non-implementation of a set target for insurance coverage.

1.4 JUSTIFICATION OF THE STUDY

Essentially, Insurance companies' consolidation, particularly, the recapitalization policy is intended to resuscitate the economy for a more vibrant operation. Such a policy seeks a higher level of financial strength for the insurance companies to be able to undertake higher risks in the eyes of insuring public. Given that the insurance companies were mandated to share up their minimum capital base from N150million, N200million, and N350million to N2billion,N3billion and N10billion respectively across the re-insurance businesses attaining the resuscitation objective become more even more challenging. The pity state in Nigerian scenario is that with a population of about 150million people, less than 5% are insured.

This study is expected to draw the attention of researchers to the concept of insurance consolidation and their importance for overall welfare of the citizens.Morealso,it will contributes to the existing body of knowledge in the areas of definition, quantification and test for the demand for and supply of insurance services. Finally, it is hoped that future researchers on this subject of insurance consolidation will find the study useful as a reference material in formulating policies that relates to insurance companies.

1.5 SCOPE AND LIMITATION OF THE STUDY

The study is an empirical analysis of an evaluation of the Nigerian Insurance Industry Consolidation and its impact on the economic growth. It covers the period between 1988-2008 and is subdivided into three periods. Pre-consolidation, consolidation and post consolidation. The study focus only on Insurance Companies and not on other players in the Industry.

The choice of 1988-2008 period is informed by the following:

(a) The period is considered significantly long enough to capture the various trends and variations in the consolidation exercise on Insurance industries in Nigeria.

(b) The periods also cover the formulation and implementation of various insurance policies and their impacts on the development of the Nigerian economy.

(c) The periods also covers the era of military regimes and civilian governments and their interests in insurance consolidation policies in Nigeria. This is to ensure a balanced assessment of issues relating to the insurance world.

(d) It is in late 1980's that Nigerian Insurance Industry started relation with foreign Insurance companies.

1.6 DEFINATION OF TERMS

(a) Annuity - An agreement by an insurer to make periodic payments that continue during the survival of the annuitant(s) or for a specified period.

(b) Insurance**: -** This is a contract in which the insurer, for a consideration or for a sum of money which is called premium, agrees to pay to the insured a sum of money or its equivalence whenever the event that was insured occurs.

(c) Re-insurance: - This is simply a secondary insurance or the process by which an insurance company places a proportion of its insured risks which it cannot bear with another insurance or re-insurance company.

(e) **Premium: -** This is the amount paid by the insured to the insurer for the insurance cover provided in the policy.

(f) **Indemnity: -** The maximum amount payable by an insurer to a beneficiary of loss. The principle of indemnity implies that the claimant does not profit from the loss.

(g) **Insurable Interest: -** The pecuniary interest a person has in a possible subject matter of insurance such as car, property or life, such that it might suffer a financial loss as a result of the happening of the event insured against.

(h) **Insurer: -** The insurance company that has undertaking to provide an indemnity, pecuniary benefits or render services.

(i) **Contribution: -** This is a doctrine, which enables an insurer to call upon another insurers, similarly (but not necessarily equally) liable to the same insured to share the cost of an indemnity. It arises when there are more than one policy in respect of the same loss and each policy is covering the interest of the same insured.

(j) **Claims: -** A demand made by an insured or the insured's beneficiary for the payment of benefits or indemnity following a loss in accordance with the terms of an insurance contract.

(k) **Cover: -** A contract of the insurance, to effect insurance, that is to cover an insured, for example, motor insurance with effect from a given time.

(l) **Cover Note: -** A document which signifies temporary acceptance of insurance of the policy document.

(m) **Consolidation**: It is viewed as the reduction in the number of economic institutions (entities) with a simultaneous increase in size and concentration of the consolidated entities in the sector (BIS, 2001); it is mostly motivated by deregulation of financial services, technological innovations, enhancing business operation and emphasis

on shareholder value, privatization and international competition (Berger et al, 1999; IMF, 2001; and De Nicolo et al, 2003).

(n) **Hazard** - A circumstance that increases the likelihood or probable severity of a loss. For example, the storing of explosives in a home basement is a hazard that increases the probability of an explosion

(o) **Policy** - The written contract effecting insurance, or the certificate thereof, by whatever name called, and including all clause, riders, endorsements, and papers attached thereto and made a part thereof.

(p) **Reinsurance** - In effect, insurance that an insurance company buys for its own protection. The risk of loss is spread so a disproportionately large loss under a single policy doesn't fall on one company. Reinsurance enables an insurance company to expand its capacity; stabilize its underwriting results; finance its expanding volume; secure catastrophe protection against shock losses; withdraw from a line of business or a geographical area within a specified time period.

(q) **Risk Management** - Management of the pure risks to which a company might be subject. It involves analyzing all exposures to the possibility of loss and determining how to handle these exposures through practices such as avoiding the risk, retaining the risk, reducing the risk, or transferring the risk, usually by insurance

(r) **Solvency** - Having sufficient assets--capital, surplus, reserves--and being able to satisfy financial requirements--investments, annual reports, examinations--to be eligible to transact insurance business and meet liabilities.

(s) **Underwriter** - The individual trained in evaluating risks and determining rates and coverages for them.

(1.7) ORGANIZATION OF THE STUDY

The study will be structured into five chapters. Chapter one gives the proposal which incorporates the background of the study; statement of the problem; objectives of the study; justification of the study; scope of the study; and definition of terms, . Chapter two will present the literature review-including conceptual, theoretical and empirical literatures. Chapter three presents the methodology used in the study including sources of data,

method of data collection and analysis, hypothesis and tests of hypothesis. Chapter four will give the analysis of the results-made up of introduction, presentation of results, results of hypothesis testing, discussing of results and policy issues of the finding. Chapter five will give the summary of major findings, policy recommendations and conclusions.

END NOTES

(1) There are two types of human societies-money economies (dominated by markets, money, financial instruments and so on) and non-money or natural economies(without market, money, financial instruments and so on)

(2) For example, if a house burn down, members of the community help build a new one, should the same thing happen to one's neighbour ,the other neighbor must help. Otherwise, neighbours will not receive help in the future.

(3) If a merchant received a loan to fund his shipment, he would pay the lender an additional sum in exchange for the lender's guarantee to cancel the loan should the shipment be stolen or lost at sea.

(4) Franklin's company was the first to make contributions towards fire prevention. Not only did his company warn against certain fire hazards, it refused to insure certain buildings where the risk of fire was too great, such as all wooden houses.

CHAPTER TWO

LITERATURE REVIEW

2.1 INTRODUCTION:

In welfare economics emphasis are placed on the evaluation of alternative economic situations (states, configurations) from the point of view of society's well being. In economic parlance, economic welfare are commonly expressed as a function of the utility levels of all members of the society. While the criteria for judging social welfare might be an ordinal index, utilities of individuals concerned must be cardinal and at least unique except for its origin and units of measurement.

With the evaluation of insurance activities as part of measures to enhance social and economic welfare, there came the need to ensure vibrancy of operations in the insurance services sub sector. Insurance business in Nigeria has evolved over the years with many legislation and regulations. The National Insurance Commission (NAICOM) act No.1 of 1997 and the insurance act No 1 of 2003 currently govern the conduct of insurance business in Nigeria.

The National Insurance commission has the responsibility for the implementation of both Acts. The insurance Act 2003 provides that, the regulatory authority (NAICOM) may from time to time, review the capital requirements. The Nigerian Government through NAICOM prescribed an increase in the minimum paid up capital of insurance companies to N2 billion for life insurance,N3 billion for general business,N5billion for composite and N10 billion for Re-insurance companies. These reforms of recapitalization and consolidation were aimed at building public confidence in the sector and enhance human capacity alongside international competitiveness of local operators.

Prior to the above minimum requirement, were over 107 insurance companies, including 4 local re-insurance. With the recapitalization policy, companies rose to the challenge of enhancing their position through mergers, acquisitions and fresh capital injection from foreign investors. For instance,

in 2007,the insurance industries premium stood at N105.38 billion as against N95.01 in 2006 which is an increase of 10.9%, while the paid up capital increased from N73.66 billion in 2006 to N104.19 billion in 2007 representing an increase of 41.5%.Similarly shareholders fund rose from N175.14 billion in 2006 to N284.9 billion in 2007 representing an increase of 62.21%.

2.2 CONCEPTUAL LITERATURE

In conceptual term , Insurance is a contract in which the insurer for a consideration or for a sum of money(usually called the premium) agrees to pay the insured(the beneficiary) a sum of money or it's equivalent whenever the event that was insured against occurs. The development of modern insurance activities saw a transition from the earliest "matter of convenience" to a modern day "matter of urgency" as every human society attempts to maximize welfare. This accounts for the centralization and regulation of insurance activities with the primary responsibility assumed by the government's insurance departments. Such a centralization and regulation policies of the state is aimed at reducing the consumer's information asymmetry while trying to overcome the problems of hazards functions, and increasing transparency of operation with a view to ensuring vibrancy in the insurance market. This solution to information asymmetry is a self selecting contract that ensures a reliable signal of insurer's solvency.

In their writing, Rees,Gravette and wambach (1999) argues that such a reliable signal can be provided by a regulating agency, thus increasing transparency in the market with the extension of this arguement by Spence (1973,1974) to include product quality.

However, Benson(2000) disputes the necessity for this ex-ante government regulations by arguing that insurance customers basically face the same information conditions as do buyers of other consumption goods. This happen if there is a customer demand for further information or if competitors can differentiate from each other by providing more information on their product quality, a self regulatory solution to information problem can be sought. In the insurance market, there exists inner market solutions

that helps to reduce information deficits such as rating operators. Hence self regulations might provide customers with reliable information and establish market discipline.

In every insurance contracts, there are fiduciary elements in which the insured pays premium in expectation of receiving future payments should some definite events occur. If the event does not occur, there will be no claim and thus, no payment is expected. Since the future is unknown, customers cannot judge product quality even after signing the contract. Hence, Benson's comparison with other consumption goods does not hold. If a self regulation(such as rating agencies) does not ensure customer information, government intervention to provide a signal of insurance quality seems justified.

During the contract period, the insurance customer is vulnerable to moral hazard of a "risk shifting" behavior of the insurer. A possible solution for the moral hazard problem is a specific contract that is designed to transfer a portion of insolvency risk to the shareholders. The risk position of the shareholders is changed by the minimum capital requirements. In this insolvency case, Spencer(2000) argues that the shareholders looses the capital and become responsible for incurred losses. This position was derived from the Benjamin Franklin(1752)'s Philadephia contributorshi p for the insurance of hoses from loss by fire in which the company not only warned against certain fire hazards, but refused to insure certain buildings where the risk of fire was too great, such as all wooden houses. The motive was to avoid the transfer of insolvency risk to the shareholders.

Another way to prevent this type of risk is by continuously monitoring the insurer's behavior, especially in the case of long term contracts such as life insurance. Monitoring when combined with insurer's interest in continuing sales, reduces the incentives for risk shifting behavior. However continuous monitoring can be very costly for a single customer. As Llewellyn(1999) and diamond(1984) posited, economies of scale and enhanced efficiency can be achieved when monitoring is delegated to a monitoring agency while Benson(2000) argues that there is no reason why this monitoring should be

done by a government agency. He posited further that there are efficient market-solutions for monitoring the behavior of financial services firms, achieved through rating. Thus in the event of ex-ante asymmetries, regulations is aimed at monitoring insurer's behavior which would be justified if self regulation does not ensure reliable monitoring or if the monitored industry is able to influence the process of monitoring.

Apart from monitoring objective of regulation and centralization of insurance activitities, there is the second objective of reducing negative externalities of insurer default. While the economic rationale for regulation in the presence of externalities is include unpriced effects in the pricing mechanism or to ensure that production and consumption are achieved by legal means, such negative externalities resulted from the information asymmetry between the customer and the insurance company.

Reduction in the information asymmetry on the part of consumers will help to internalize insolvency risk into the pricing mechanism so as to reduce the negative effects of default on competitors. In absence of private solutions for reducing negative externalities, remedies may be sought for, through public policy. As noted by mankiw(2007),in the case of insurance, regulation can increase market efficiency by instituting a "command and control policy". Consequently, regulatory means should be employed to secure positive externalities of insurance contracts and to diminish the negative externalities of insurer's default.

A third and more fundamental objective of insurance regulation is to safeguard the competitive adequacy of operators. This objective is derivative of a common place economic theory of perfect competition. Market outcome of insurance activities depends more crucially on adequate competition for customers between insurance service providers. Thus, as carmihael(2001) noted, regulatory action should be capable of safeguarding this level of competition by lowering existing barriers to market entry and exit. Munch and smallwood(1980)had similar position that solvency regulation can have a substantial effect on contestability, which need to be be carefully analyzed to prevent additional market barriers. This will make

regulation capable of analyzing the effects of any regulatory measures on economies of scale and scope so as tom prevent excessive concentration of market power.

Only companies that were so specially registered after their incorporation under the companies Act could operate as insurance companies with their proposed field(s) of operation. In addition the companies were required to submit their audited accounts to the registrar of insurance. Kasim(2006)stated that all these were in attempt to checkmate the sharp practices within the insurance sector.

The promulgation of the Nigerian Insurance companies decree of 1968 introduced a more stringent requirement needed to checkmate unethical practices in the insurance companies. The decree required that each company to produce certified true copies of premium rates, rating plan, rules and standard policy forms for each classes of insurance, together with a certified copy of audited accounts showing the financial position of the company. This decree gave birth to the regulation of the paid up share capital of the insurance companies that operates in the country. Kasimu(2006) reported that N100,000 for those transacting business in all classes of insurance and N50,000.00 for those concerned with only life insurance.

Despite these requirements, the market remained open as operators are seeing entering and leaving the industry at will. Kasimu(2006) reported further that this entry and exit practice resulted in all manner of industries doing the business of premium collection to satisfy own ends but once faced with claims obligation, they either blatantly refused to pay, pay low compensation, or even go into self-liquidation on one protest or another. This act resulted into the introduction of brokers, loss adjusters, agents and insurers by the government to protect the insuring public who are the weaker party to the bilateral contracts of insurance.

2.3 THEORITICAL LITERATURE

Theoretically, the concept of insurance can be linked with the theory of perfect competition. The fundamental basis of insurance operations lies with the assumption that buyers and sellers of insurance coverage have perfect information about each other before signing an insurance contract. While it can be argued, that this assumption may not be tenable in real world, the effects of information asymmetry can be organized in accordance with the temporal appearance of participants before an insurance contract is signed. This will give the consumer (the buyer of insurance coverage) the ability to evaluate all competing products within a perfectly competitive market situation. Consequently, the consumer may act as both a creditor (paying the premium) to the insurer, and as debtor (by paying in advance for future conditional payments).These dualistic characterization of signed contract makes the insurer's default probability highly relevant to product quality. In their writings, Doherty and Gauven(1986) carefully examine the issue of insolvency in insurance market .They opined that a fully informed customer will take insolvency risk into consideration and accept insolvency risks only with a premium discount Also, wakker, thaler and Tversky (1997) show the effect of small insolvency risks on insurance premium in which they posited that due to information asymmetry, the ruin probability is not totally known to the customer before signing a contract. Similar position was held by Akerlof(1970),Rothschild and Stiglitz(1976).Consequently, consumers are not able to judge any important quality aspect of the insurance product at the point of purchase. This asymmetric information can lead to adverse selection of insurance companies which is capable of preventing deals from taking place.

Accordingly, Greenwald and stiglitz(1986),Eric and Stephen(2004) posited that when imperfect information exists in the market, benefits from insurance cover are not constrained in a pareto efficient state. In economics, imperfect information as pecuniary externalities have real welfare consequences. In traditional term, these pecuniary externalities were ignored by economists because one person's loss through market activities is another person's gain which will ultimately resulted in a no welfare net loss.

However, with imperfect information, this result does not hold in reality. This is because, the fact that insurance firms can only partially screen high risk from low risk applicants which can imply that the low risk applicants are penalized by higher premiums. In the event of imperfect information, the result of the market place are not pareto efficient. However the ability of the government to improve on the situation by inducing a pareto-improving exchanges depends on the volume and quality of information available. Acording to Stiglitz(2000),the results change the nature of analysis and can justify government intervention in the market. At times the government may be able to improve on the market outcome because of information constraints. Thus, the ability of the public sector to absorbs and spread information costs is likely to lead to positive information roles for government entities as in providing general public goods.

On the contrary, if a contract make it possible for at least one of the parties to change behavior during the contract period, moral hazards are likely to occur. Introducing the hidden action problem, Arrow(1971) attempt to model moral hazard in the insurance market in which he posited that the hidden action problem arises when action of one party to a contract are not immediately observable by the other(s).Also Stiglitz and Welss(1981) presented a moral hazard case in credit market. On the whole, insurance contracts are vulnerable to moral hazard from insurance company's management because insurers are able to change their behaviors after signing the contracts in a way that goes unnoticed by the insured.

Generally, the insured is not able to observe the change in behavior without incurring some cost. As Jenson and Meckling(1976) noted, the incentive to changes in behavior derives from the conflicting interest of shareholders and debt holders. The shareholders of an insurance company will profit from shifting risks to the disadvantage of the debt holders.(the insured).The owners of insurance company's equity capital are in long run gainers. Hence, menton(1974,1977) has argued that an increase in corporate risk such as asset volatility, will increase the value of the call option, leading to moral hazard which will consequently cause some significant market distortions.

These distortions are corrected with some appropriate policy reforms-predicted upon the need for re-orientation and repositioning the insurance markets so as to attain an effective and efficient state. As Ahmadu(2006) noted, reforms are carried out either through government institutions or private enterprises, and become inevitable in the light of the global dynamic exigencies and emerging land scapes. While several authors like Rees,Gravelle, and Wambach(1999) and spancer (1973,1974) have argued in favour of reforms as providing reliable signal through the regulatory agencies of government, others like Benson(2000) disputed the necessity of ex-ante government regulations, arguing that insurance customers basically do face the same information conditions as do buyers of other consumption goods, and a self regulation will likely occur as competitors of insurance services can differentiate from each other product quality through information.

2.4 EMPIRICAL LITERATURE:

Empirically, results obtained from the consolidation of insurance companies around the world have been mixed. While insurance consolidation exercises enhanced growth and development in some countries, its outcome in other countries is that of under development. For example in Morocco,the consolidation exercises embarked upon in the late 1990s lead to the establishment of two large entities-RMA-Watanya and AXA Assurance Maroc. While the RMA-Watanya emerged as a result of the double merger of Al-Watanya and Alliance in 2000,before it emerged again with RMA in 2005 which conferred on the company, the tittle of being the largest insurance company in Morocco at the end of 2005 in terms of premium payment, the AXA Assurance Maroc originated from the merger of the companies Africaine and AXA-Al Amane.

In 2006,the Moroccan Insurance Industry went through an important Consolidation phase which brings the number of operating firms to five companies.

During the consolidation, Sahum acquired Essanda, which has long been a major shareholder in CNIA.The consolidation exercise saw RMA-Watanya-

the largest disbursing MAD 2.88 Billion in 2005 and is closely followed by AXA Assurance Maroc with MAD 2.19 Billion. Others are Wafa assurance with MAD 1.62 Billion,CNIA with MAD 1.14Billion, and Essanda with MAD 887.4 Million.There came a new entity (CNIA-Essaada) with a total of MAD 2 Billion,which ranked third,out-ranking the Attianwafa Bank's insurance arm(Attantasanad) with MAD 1.58 Billion.

The development of consolidation in the case of Algerian Insurance market saw a rather slow-growing economy that it was initially conceived to be. Despite operating in a much bigger economy, Insurance sector in Algeria is still smaller compared to its neighboring Morocco and Tunisia in terms of its value and growth. In December 2005,the revenue generated by Insurance companies in Algeria amounted to DZD 42.2 Billion which represents a 14% rise over the preceding year(2004).The goal of its consolidation was to re-enforce the government and management techniques in all state owned companies along side cleaning up and streamlining of the auto insurance branch with the help of foreign expertise and finally, the establishment of tax incentives that will enable the flow of money into the sector.

In the Nigerian case, Insurance began with the British Merchants who introduced the business in the first quarter of the 20th century. With the coming to Lagos of Royal exchange Assurance in 1921,Insurance business was monopolized by the company for 35 years up till 1949.According to Kassim(2006),two other British Insurance companies entered the Market and by 1960 their number had increased to 25.Within this period, there was virtually no form of government regulation or control. This was due to the prevalence of foreigners whose home laws were believed to have adequately take care of the operations of the companies in the colony. The only national law of considerable significance on insurance were the Motor Vehicles(Third Party) ordinance of 1954 and the Motor vehicles of Act of 1958.As noted by Kassim(2006),once a company is incorporated, it could start operating as an Insurance Firm.

Insurance regulation in Nigeria began with the marine insurance ACT OF 1961,the Insurance Act of 1961 and the Insurance(Miscellaneous Provision)

Act of 1964.The regulation stipulates that only companies that were so specifically registered after their incorporation under the companies act could operate as insurance companies in accordance with their proposed field(s) of operation. The law equally stipulates that Insurance companies should submit their audited account to the registrar of Insurance. Kassim (2006) opined that all these were in attempt to checkmate the sharp practices within the Insurance sector.

Empirically, most of the research findings on Insurance businesses rest more on methodological issues.Miller (2008) applied the traditional and generalized verson of the Capital Asset Pricing Model (CAPM) to derive a class of premium principle which was in conformity with Buhlman's (1980) economic Premium principle. On the other hand, Sharpe (1964) and Lanter(1965) derived the camp based on the mean-variance analysis with a conclusion that equilibrium conditions on capital market are a central issues in the theory of corporate Finance. Later the CAPM was generalized to the case of risk evaluation by Newman utilities as found in the Menton(1982).

There are only a few recent papers in which elements of risk theory have been combined with models of corporate finance and welfare economic theory. In their separate studies, Buhlmann(1980,1984) and Lienhard(1986) derived a class of premium principles by applying a general equilibrium approach to the Insurance market. Kahame(1979) stressed the importance of investment income on premiums and made a first step in order to apply the traditional capital assets pricing model to premium calculation.

Also, Miller(2008) attempted to unify the ideas of articles mentioned above by means of simple model and found that the class of premium principles corresponds exactly to the class of premium principles derived by Buhlman(1980) and Lienhard(1986) and observed that, at least, risk theory and theory of corporate finance lead to perfectly compatible conclusions. Some efforts were made to study the insurance operations in Nigeria. In its study, BM(2008) revealed that Nigeria's over all insurance business environment (IBER) was 34.4% compared with South Africa, Morocco, Egypt and Tunisia with 67.7%,45.3%,42.2%,and 39.2% respectively. The

implication of this survey is that Nigeria's overall Insurance sector is the least attractive of any of the Africa's countries covered by BMI in 2008.To this end, there is the need for consolidation for the risk adjusted capitalization to enhance the ability of the Insurance companies in Nigeria to adequately cover for Policy holders in the world of increasing risks. The apparent lack of broad based ownership together with a limited capital accounted for the fundamental short comings of Insurance sector in Nigeria.

In some other methodological studies, Mitchel-et al (1999) studying the mortality rates or life expectancy to determine the type of annuity to purchase, showed that for a life cycle individuals with plausible risk aversion and mortality uncertainty and no annuity income, purchasing an annuity may raise a life time expected utility even if the expected present discounted value of payouts from annuity is no more than 75% of the purchase price .In this case, where both compulsory and Voluntary annuity markets exists, adverse selection will operate differently because in the voluntary annuity market, those with high expected mortality have the option of not purchasing it at all while in the compulsory market, the only option is for them to purchase an annuity.

In other studies, Evans(1999) model insurance company as a Multi-product firm which utilizes labour, Capital, and entrepreneurial skills as measured by amount of commission and other expenses paid on Insurance Policies to produce a certain level of output. Using Insolvency Model, Doherty and Gaven (1986) examined Insurance market behavior and concluded that fully informed customers will take insolvency risk into account and accept insolvency risks only with a premium discount. Equivalently, Wakker Thaler and Trersky(1997) show the effect of even small insolvency risks on Insurance premiums and conclude that customers do not always judge the important quality of Insurance product at the point of purchase.

2.5 INSURANCE REGULATIONS AND ECONOMIC OBJECTIVES

REDUCTION OF INFORMATIONAL DISADVANTAGES

The first objective of insurance market regulation is to reduce the consumer's informational disadvantage. Information about the financial health of an insurance company is asymmetrically distributed. Problems arising from ex ante information asymmetries can be solved by increasing transparency in the market or by collecting credible information about insurer quality. A solution to this information asymmetry would be a self-selecting contract or a reliable signal of insurers solvency. Rees, Gravelle, and Wambach (1999) argue that such a reliable signal can be provided by a regulating agency, thus increasing transparency in the market (on signaling product quality: Spence, 1973, 1974).

However, Benston (2000) disputes the necessity of ex ante governmental regulation, arguing that insurance customers basically face the same informational conditions as do buyers of other consumption goods. If there is a customer demand for further information or if competitors can differentiate from each other by providing more information on their product quality, there will likely occur a self-regulatory solution to the information problem. In the insurance market context, there are inner market solutions that reduce informational deficits. For example, rating agencies provide signals of insurer quality. Hence, self-regulation might provide customers with reliable information and establish market discipline. Insurance contracts contain fiduciary elements. The insured pays a premium in the expectation of receiving future payments should some definite event occur. If the event does not occur, there will be no claim and thus no payment. Because,

usually, the future is unknown, customers cannot judge product quality even after signing the contract as a result, creates a substantial public interest in insurance customer information. Hence, Benston's comparison with other consumption goods does not fully hold. If self-regulation, for example, by rating agencies, does not ensure customer information, government intervention to provide a signal of insurer quality seems justified.

During the contract period (ex interim), the insurance customer is vulnerable to moral hazard by risk-shifting behaviour of the insurer. A possible solution for the moral hazard problem is a specific contract design that transfers a portion of the 10 insolvency risk to the shareholder. The risk position of the shareholder is changed by minimum capital requirements. In case of insolvency, the shareholder loses this capital and becomes responsible for incurred losses (Spencer, 2000). Another way to prevent this risk is by continuously monitoring insurer behavior, especially in the case of long-term contracts such as life insurance contracts. Monitoring, in combination with the insurer's interest in continuing sales, diminishes incentives for risk-shifting behaviour. However, in general, continuous monitoring is very costly for a single customer. To achieve economies of scale and enhance efficiency, monitoring can be delegated to a monitoring agency (Llewellyn, 1999; Diamond, 1984). Benston (2000) argues that there is no reason why this monitoring should be done by a government agency. In his opinion, there are efficient market solutions for monitoring the behavior of financial services firms, for example, rating agencies. Thus, in the situation of ex ante asymmetries, regulation aimed at monitoring insurer behavior would be justified if self-regulation does not ensure reliable

monitoring or if the monitored industry is able to influence the monitoring process.

REDUCTION OF EXTERNAL EFFECTS

The second objective of insurance market regulation is to reduce the negative externalities of insurer default. The rationale for regulation in the presence of externalities is to include unpriced effects in the pricing mechanism or to ensure that production and consumption are achieved by legal means. Some of the described negative externalities result from the informational asymmetry between the customer and the insurance company. Reducing the consumers' informational disadvantage will internalize insolvency risk into the pricing mechanism and so reduce the negative effects of default on competitors. If there are no private solutions for reducing negative externalities, remedies may be sought through public policy. In the case of insurance, regulation can increase market efficiency by instituting a "command-and-control policy" (Mankiw, 2007). Thus regulatory means should be employed to secure positive externalities of insurance contracts and to diminish the negative externalities of insurer default. 11

Systemic risk of insurer default is of increasing importance. Regulatory action should therefore be directed toward sustaining systemic stability and the maintenance of safe and sound financial institutions. To counteract the effects the negative externalities of the insurance cycle have on the customer, regulators should take into consideration the possible cyclical effects of any regulatory measure.

SAFEGUARDING COMPETITIVE ADEQUACY

The third objective of insurance market regulation that can be derived from economic theory is the safeguarding of competitive adequacy. Market outcome of insurance markets depends on adequate competition for customers between insurance providers. Regulatory action should safeguard this level of competition by lowering existing barriers of market entry or exit (Carmichael, 2001). According to Munch and Smallwood (1980), solvency regulation can have a substantial effect on contestability, which needs to be carefully analyzed so as to prevent additional market barriers.

In addition, regulators need to analyze the effect of any regulatory measure on economies of scale and scope so as to prevent excessive concentration of market power.

2.6 INFORMATION ASYMMETRIES AND INSURANCE BUSINESS

The theoretical concept of perfectly competitive insurance markets assumes that buyers and sellers of insurance coverage are perfectly informed about each other and the signed contract. In practice, those engaging in insurance market transactions usually have imperfect knowledge. The effects of asymmetrically distributed information can be organized according to their temporal appearance before signing the contract (ex ante effects), during the policy period (ex interim effects),or after maturity of the contract (ex post effects). In the context of insurer solvency regulation, ex post effects, such as costly state verification, are of no specific relevance. Due to asymmetrically distributed information, the ruin probability is not totally known to the customer before signing a contract (On the problem of ex ante asymmetrically distributed information, see Akerlof, 1970; Rothschild and Stiglitz, 1976). Thus the customer is not able to judge an important quality aspect of the insurance
product at the point of purchase. This information asymmetry can lead to an adverse selection of insurance companies, preventing deals from taking place or even extinguishing market activities.

If a contract makes it possible for at least one of the parties to change behavior during the contract period (ex interim), moral hazard is likely to occur. Arrow (1971) introduced the hidden action problem by modeling moral hazard in insurance markets. Stiglitz and Weiss (1981) present a moral hazard case in credit markets. The hidden action problem arises when actions of one party to a contract are not immediately observable by the others. Insurance contracts are vulnerable to moral hazard from the insurance company's management because insurers are able to change their behavior after signing the contracts in a way that goes unnoticed by the insured. Generally, the insured is not able to observe the change in behavior without incurring some cost. The incentive for a change in behavior derives from the conflicting interests of shareholders and debtholders (Jensen and Meckling, 1976). The shareholders of an insurance company will profit from shifting risk to the disadvantage of the debtholder, that is, the insured. The owners of the insurance company's equity capital are in a long call position on the company's future value (Merton, 1974, 1977). An increase in corporate risk, e.g., the asset volatility, increases the value of that call option. Thus there is an incentive for shareholders to increase risk during the contract period and the resulting moral hazard can cause significant market distortions

2.7 EXTERNALITIES

Externalities can occur at the microeconomic level if the consumption or production of a good has spill-over effects to individuals not directly involved in the transaction. For example, the main function of car insurance is to compensate a third party in case of any damage caused by the insured driver. Thus the beneficiary of the insurance is not only the insured but every other person engaging in road traffic because the monetary risk of participation in road traffic is reduced. The decision to purchase insurance has positive externalities on the risk position of third parties (see Baldwin and Cave, 2002), In addition, risks transferred to insurance companies by customers are usually those that the customer, and society, considers to be very important and serious. For example, in a worst-case scenario, default by a life insurer will leave the insured's family without any income, which will result in high external costs for society.

2.8 CONSOLIDATION AND THE NIGERIA'S INSURANCE INDUSTRY-AN OVERVIEW

The first Insurance business in Nigeria, the Royal exchange Assurance company Ltd was established in Lagos in 1921.This company enjoyed the monopoly of Insurance business for almost 30 years before two other British Insurance companies entered the market in 1949.Kassim(2006) reported that by 1960,the number of insurance companies had increased to 25.Within these periods, the Industry was free from any form of government regulations as a result of its domination by the expatriates who colonized the country. The only national law of considerable significance on the Insurance were the motor vehicles (third party) ordinance of 1954 and motor vehicles (third party) act of 1958.With the marine insurance Act of 1961,the Insurance company act of 1961 and the Insurance(Miscellaneous Provision)Act of 1964, the regulation of Insurance Industry began in Nigeria.

In the 1968 promulgation of Nigeria's insurance decree which introduced some stringent measures to curtail the unethical practices in the Industry, the paid up capital of insurance companies operating in the country was raised to N100,000 (for all those transacting all classes of Insurance business) and N50,000(for all those concerned with only life insurance.

There followed some periodic regulations that were aimed at sanitizing the operations of Insurance service providers. By June 2005,the Federal Government initiated the recapitalization in the Insurance sector which is aimed as resuscitating the Industry for a more vibrant position. The exercise sought a higher level of financial strength for the Insurance companies to be able to undertake bigger risks in the eyes of the insuring public. The policy requires that all Insurance companies should as a matter of necessity, shore up their minimum capital base from N150m,N200m and N350m to N2bn,N3bn and N10bn respectively.

By November 14,2007, the National Insurance Commission(NAICOM) released the list of 48 Insurance companies and one re-insurance company that have crossed the consolidation hurdle. In August,2008,the commission also re-issued the licenses of NICON Insurance Plc and Nigeria Reinsurance corporation to bring the number of companies to 51.At present, the composition of the operating firms in the Industry include two re-insurance companies. Seven Insurance companies and 19 composite Insurance companies.

The 2007 and 2008 could be described as years of abundance for the companies, following their successes recorded in their wealth. Unfortunately, the harsh global realities of the periods made it impossible for them to utilize their acquired wealth. However, major events that trailed the recapitalization which had continued to transform the sector can be analyzed in different perspectives judging from their portfolio capitalization return to shareholders, branch expansion, product development, human capital, impacts of statutory policies as well as other challenges.

During the exercise, about $600m came into the sector as direct foreign Investment through the Nigerian Stock exchange. This was unprecedented in the annals of Insurance operation in Nigeria. More benefits are expected to be reaped in the course of the consolidation exercise.

2.9 STRATEGIC OBJECTIVES OF THE REFORMS IN THE INSURANCE SECTOR :

(1) Become the safest insurance market in Africa;

(2) Obtain a strong positive image of the insurance sector:

(3) Become the fastest growing market in Africa;

(4) Make the Nigerian insurance market the first choice in Africa; and

(5) Build a single West Africa insurance market.

2.10 GENERAL OBJECTIVES OF INSURANCE CONSOLIDATION IN NIGERIA

- -To increase the industry's low retention capacity, which had stunted its growth.

Government was especially concerned about low local underwriting capacity for big
ticket risks in the oil and gas, aviation, marine and other special risk sectors and was
determined to dam the huge foreign exchange outflow engendered by the situation

- To attract foreign capital infusion into the industry for enhanced premium growth

and profitability

- Achieving a consolidation that will produce companies capable of meeting claims

obligations and compete at the continental and global levels

- To enable operators to attract the wherewithal for strategic investments in human

capital development – ie, to attract, train and retain professionals able to utilize new
technologies for greater efficiencies

- Creating a competitive environment which leads to brand activities, increased investment

and better public awareness of the benefits of insurance to society at large

- Achieving the necessary economies of scale that will make insurance affordable

and accessible

- Encouraging the industry to leverage on synergies from mergers and acquisitions

and other alignments to achieve superior product innovation, deeper market penetration and product distribution.

END NOTES

1. An economic state or configuration is a particular arrangement of economic activities and resources of the economy towards the attainment of an Individual or societal welfare.
2. Negative externality occur when the consumption or production of a good causes a harmful effect on a third party. With negative externality, social cost is usually greater than private cost.
3. Positive externality occur when the consumption or production of a good causes a benefit to a third party. With positive externality the benefits to the society is usually greater than private benefits.
4. The CAMP formular is an equilibrium condition which relates risk premium to the covariance between the returns on the Market portfolio and the corresponding assets.

CHAPTER THREE

METHODOLOGY

3.1 INTRODUCTION

When the Federal Government initiated the policy of recapitalization in the insurance sector in 2005,it was aimed at resuscitating the ailing insurance companies from its comatose state to a more vibrant position. Its design was to sought a higher level of financial strength for the insurance companies to be able to undertake bigger risks as well as engender more confidence in the eyes of the insuring public. Five years on, the trends in the insurance industries are revealing some developments which indicate that the sector is coming of age, even though, it is still grappling with some major challenges.

It should be recalled that the insurance companies were asked to shore up their minimum capital base from N150million, N200million, and N350million for life, general and reinsurance businesses to N2billion, N3billion and N10billion respectively. By November 14, 2007 the National Insurance Commission released a list of 48 insurance companies and one reinsurance company that have successfully scaled through the recapitalization hurdle.

By August 2008,the commission also raised the licences of Nicon Insurance PLC and Nigeria Re-insurance corporation, thereby bringing the total number of companies operating in the country to 51.At the moment, the composition of the operating firms in the industry, include two reinsurance companies, seven life insurance companies, twenty three general insurance companies, and Nineteen composite insurance companies. From the 2007 and 2008 financial reports of the company, it could be said that the period particularly 2007 was a year of abundance for companies as they were seen "swimming" in their newly accumulated capital, which they were not certain on how to channel their profits into investments. The harsh effect of the global economic meltdown in 2008 resulted in a cankerworm for majority of the companies as they were unable to utilize their acquired wealth.

However, some major events that trailed the recapitalization, which had continued to transform the sector can be analyzed in different areas which includes Investment Portfolio capitalization, returns to shareholders, branch expansion, product developments, human capital, impact of statutory policies and other operational challenges.

3.2 SOURCES OF DATA

The research as an analysis of an evaluation on the impact of the Nigerian Insurance Industry consolidation of 2005.The study is predicated on the fact that despite all policies and programmes put in place to ensure that the insurance companies are resuscitated towards vibrancy, more than70% of private properties are yet to be insured while only 5% of the total population of Nigeria are insured while only 10% of all existing properties at the Federal, State and Local Government levels are insured.

Therefore, the data collected for this work are on annual basis and it covers the period 1988- 2008.The data collected are on the GDP, Premium, Indemnity, Capital, Labour, Consolidation and openness. These data are collected from Annual reports of National Insurance Commission, CBN Statistical Bulletins, Annual abstract of statistics from National Bureau for Statistics.

The GDP is the dependent variable while the independent variables are the premiums, indemnity, capital, labour, degree of openness and dummy variable (consolidation)..

3.3 METHOD OF ANALYSIS.

The study employs an econometric technique as its methods of analysis. The process involves measuring the stochastic (non-exact) relationship between the regress and the regressor variables of interest. This entails estimating the parameters to measure, test and validate economic relationships based on the

prediction of neoclassical model. The model will be estimated using the statistical packages for social sciences (SPSS) version 13.0

The implication of the findings is for the design of public policy to ensure that lives and property are insured to the fullest. The choice of all conditioning variables were limited in other to avoid the problems of multicollinearity associated with regressing too many explanatory variables on a single regressand since most econometric variables are inter related and to avoid spurious correlation. The evaluation of this study is conditioned on the generally accepted criteria apriori, statistical and econometric.

The apriori criteria are based on the principles of economic theory concerning the possible relationship between dependent and independent variables. The statistical criterion is based on the dictates of statistical theory and it concerns the value of R^2 and the statistical significance of the parameter estimates. On the other hand, the econometric criterion is based on the principle of econometric theory which ensures that parameter estimates meet the desirable properties of best, linear, unbias and efficient estimation.

3.4 MODEL SPECIFICATION

The model specification is the CAMP (Capital Asset Pricing Model) based on the assumption that all investors have the same expectations concerning the means, standard deviations and covariance between all securities. The equation for the capital market line is

$$Ep = Rf + \frac{Em - Rf}{\delta m}\delta p$$

..... (1)

Where:

E: Denotes expected value while d denote the standard deviation.The subscripts p and m denote a portfolio and market portfolio respectively.

But the expected return of each individual investment under equilibrium in the CAMP must satisfy the following equation:

$$E_t = R_f + \frac{Em - Rf}{\delta^2 m} \delta tm$$

……(2)

Where dtm represents the covariance between return on security i and the return on the market portfolio. Equation (2) means that the expected return on the individual security equals the return on the risk free asset plus a proportional risk loading.

Assume that the insurer holds an investment portfolio composed of n securities(assets).The amount invested in activity i Sxi(i=m+1,……m+n) and the rate of return on this activity is a stochastic variable V_t.The total profit of the firm,Y,is

$$Y = \sum_{i\ldots,m+n}^{m+n} XiVt - \sum_{i=1}^{M} XtVt \quad \ldots\ldots\ldots\ldots(3)$$

Where the two summation in the right hand term express the aggregate investment [1] profit and the total underwriting loss (profit) respectively.Dividing bothsides of the equation by the equity capital K gives:

$$Vy = Y/K = \sum_{1=m+1}^{m+n} \frac{Xt}{k} Vi - \sum_{i=1}^{m} \frac{Xt}{k} Vt \quad \ldots\ldots\ldots\ldots\ldots(4)$$

Let Xt = Xt/K denote the premium and investment relative to capital.Adding a subscripts j to the element of the equation in order to relate it to a certain insurance company j gives

$$Vgf = \sum_{i+m+n}^{m+n} xifvt - \sum_{i+1}^{M} xtfVt \quad \text{----------(5)}$$

Note that Vt are assumed to be identical for all insurance companies in the market.Since the CAMP suggests that the expected return on firm j shares is related to it's systematic Bj,it follows that:

$$E\,(Vyf) = Rf + (E_m - R_f)\,\beta_j \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots(6)$$

Taking the expected value of the equation (5) substituting into equation(6) yields;

$$E(V_y) = \sum_{1=m+1}^{m+n} Xtj\,E(Vi) \;-\; \sum_{i=1}^{m} Xif \sum(Vr) = Rf + \beta j(Em - Rf) \ldots\ldots\ldots\ldots\ldots(7)$$

Note that the systematic risk of a portfolio is a linear combination of the systematic risk elements of it's component.Therefore,the systematic risk of the insurance firm j is a weighted average of the systematic risk of all underwriting and investment activities.That is

$$Bj = \sum_{1=m+1}^{m+n} Xif\beta i \;-\; \sum_{i=1}^{m} Xti\beta r \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots(8)$$

Subtracting equations (8) from (7) and eliminating the subscript j for the simplicity of notation yields:

$$\sum_{1=m+1}^{m+n} E(Vi) \;-\; \sum_{i=1}^{m} XiE(Vi) = Rf + [\sum_{i=1}^{m+n} xi\beta r - \sum_{i=1}^{m} xi\beta r][Em - Rf] \ldots\ldots(9)$$

Since investment activities obey the same capital market equilibrium relationships,the expected return on every investment satisfies the equation

$$E(Vi) = Rf + \beta i\,(Em - Rf) \quad i = m+1, \ldots\ldots, m+n \ldots\ldots\ldots\ldots\ldots\ldots(10)$$

And the return on the entire investment portfolio is given as:

$$\sum_{1=m+1}^{m+n} Xi\,E(Vi) = \sum_{1=m+1}^{m+n} Rfxi + \sum_{1=m+1}^{m+n} xi\beta i(Em - Rf) \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots(11)$$

Subtracting equations (11) from (9) gives the expected underwriting profit which preserves the capital market equilibrium

$$\sum_{i=1}^{m} Xi\ E(Vi) = Rf(1 - \sum_{1=m+1}^{m+n} xi) - \sum_{i=1}^{n} xi\beta i(Em - Rf) \qquad \ldots\ldots\ldots\ldots\ldots(12)$$

Assuming that each naira of premium in insurance activity i generates gi Naira of investment, the insurer's balance sheet equality[2] is expressed as

$$\sum_{1=m+1}^{m+n} xi = 1 + \sum_{i=1}^{m} xigi \qquad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots \qquad .(13)$$

Substituting equation (13) into (12) and re-arranging

$$\sum_{1=1}^{m} xi\ E(Vr) = Rf \sum_{i=1}^{m} xigi + \sum_{i=1}^{m} xi\beta r(Em - Rf) \qquad \ldots\ldots\ldots\ldots.(14)$$

However, this equation does not lead to a clear cut statement about the expected rate of underwriting loss on each individual insurance activity. Given all Bi Em, Rf and the value of xi,the equation is insufficient to determine a single set of E(Vi) (i=1,…m) and as Bigger and Kahane (1978) admit, their may be a large number of vectors that satisfy it.One possible solution in this case is that since the equation resembles the CAMP relationship,

$$E\ (Vi) = Rrgi + \beta 1[E_m - R_f\ ) \qquad i=1, \ldots\ldots\ldots\ldots m\ldots\ldots\ldots\ldots\ldots\ (15)$$

It means that the firm on the average be willing to lose on insurance activity i as much as gi times the risk-free rate,plus a risk loading proportional to it's systematic risk.

Since all firms in an economy invest in economic activities to bring the desired level of output in order to satisfy the demands of every economic unit, the final form equation is to estimate directly:

$RGDP = \alpha_0 + \alpha_1 Prem + \alpha_2 Ind + \alpha_3 Dumcon + \alpha_4 cap + \alpha_5 lab + \alpha_6 Doo + \mu$ ……..(16)

Clearly, since these variables in equation (16) do not have same unit of measurement, the usual practice would be to take the logarithm of each variable (with the exception of degree of openness which is in ratio form) and estimate linearly.

Thus the specification becomes

$Log\ RGDP = \alpha_0 + \alpha_1 logPrem + \alpha_2 log\ Ind + \alpha_3 Dumcon + \alpha_4 log\ K + \alpha_5 logL + \alpha_6 logDoo + \mu$ ……(17)

Where:

RGDP = Real gross domestic product in logarithm form,

Prem = Log of prem

Indem =Log of indemnity

Dumcon = Log of Dummy variable;assuming (0) when the consolidation policy was absent and one (1) for periods of consolidation

K =Log of gross fixed capital formation

L: Log of labour (number of economy's workforce)

Doo =Degree of openness

U = Stochastic error term

α = Constant

α_1 -α_6 = Parameter estimates.

3.5 HYPOTHESIS

Every economic activity is subject to the existence of certain structural rigidities that may inhibits smooth functioning and growth. The achievement of an activity's core mandate towards enhancing and sustaining economic imperatives of human endeavor depends more crucially on the adequacy of economic reforms and policies directed towards the attainment of an effective and efficient state.

Consequently, the null hypothesis is stated as follows:

Ho: β =0

Against Hi: $\beta \neq 0$

At αo = 0.95

With β =0 it implies that insurance companies' consolidation has no impact on the economic growth in Nigeria economy.

While $\beta \neq 0$ implies that insurance companies' consolidation has impact on the economic growth in Nigeria economy.

This hypothesis would form the basis upon which the theoretical plausibility and empirical validity on the on impact of the Insurance companies' consolidation on the aggregate performance of the economy would be evaluated.

END NOTES

1. The aggregate investment in this case produces the output (GDP) of the economy i under study.

2. That is,the requirement that assets equal the equity plus liabilities

CHAPTER FOUR

ANALYSIS OF RESULTS

4. 1.0 INTRODUCTION:

Theoretically, the economics of consolidation of the Nigeria's insurance companies was aimed as resuscitating the ailing sector and to seek a higher level of financial strength for the insurance companies with a view of undertaking a bigger risk to cover the insuring public.

With the advent of consolidation, the National Insurance Commission (NAICOM) embarked on some measures to uplift the face of Insurance in Nigeria under a project tagged "Nigeria Insurance Market Development and Restructuring Initiatives" (MDRI).

4.1.1 CONTRIBUTIONS OF INSURANCE COMPANIES TO THE GDP IN POST CONSOLIDATION ERA.

Consolidation has given Insurance companies stronger financial strength to under take bigger business risks. The Industry was able to form consortia with several insurers pooling funds together to enable them underwrite significantly large risks,especially in oil and gas,aviation,Marine etc.

Further with better capital base for the Industry, recently Government propagated some regulations in support of growth in the Industry and in the entire economy..The legislation includes

- Compulsion of all private sector organizations operating in Nigeria to enroll their employees in the National Health Insurance Scheme to boost it's resource base
- Introduction of local content for oil and gas Industry and an increase in the applicable rate from 10% to 45% in 2007
- Planned reactivation of the VISER/OSCAR sticker an initiative meant to increase the coverage of Motor vehicle insurance

All the above policies are done in order to increase the premiums earned by insurance companies and through premiums, players in the industry are able to invest in financial instruments so as to remain in a

good position to continue to meet claims obligations as and when due. This actually contributes to the GDP.

In Nigeria the non-oil sector contribution to the GDP has grown significantly over the years from 45% in 1992 to 69% in 2007.This growth is attributed to successfully concluding some key reforms including: Fiscal policy reforms, Debt management reforms, Budgetary reforms, Monetary reforms and Financial sector reforms.(Economic Intelligence Unit of the Economist).

4..2.0 CREATIVE ACTIVITIES INIATED BY THE INSURANCE COMPANIES TO EFFECTIVELY DELIVER.

One of the initiatives of Insurance companies for improved products and service delivery is the introduction of Market Development and Restructuring Initiatives (MDRI).
The MDRI project is a medium term plan of installing the first phase of the necessary reforms in the areas of Industry capacity, Market efficiency and Consumer protection in the Nigerian Insurance market. It would deepen and grow the insurance market and move the industry gross premium from N164billion (2008) to I.0 trillion 2012.

4.2.1 BENEFITS OF THE PROJECT

At the end of the plan period (2012) the following benefits are expected to be achieved by the Insurance market:

- Increase in industry gross premium from N164.50billion (2008) to N1.0trillion by 2012
- Direct project revenue of N800.0m to NAICOM from implementing the pro
- Revenue to Fire Service by way of fire service maintenance fund
- Creation of about 250,000 jobs in the insurance industry
- Lowering of insurance gap from 94% to 70%
- Increase in insurance contribution to GDP from 0.72%to over 4%
- Building consumer trust and confidence in the Nigerian insurance Market

4.2.2 "MDRI" FOCUSES ON FOUR KEY ISSUES:

(A) Enforcement of compulsory Insurance Products in Nigeria

(B) Sanitization and Modernization of Insurance Agency System

(C) Wiping-out of fake Insurance Institutions

(D) Introduction of Risked based Supervision

(A) ENFORCEMENT OF COMPULSORY INSURANCE PRODUCTS IN NIGERIA

There are 6 insurance products made compulsory by law by the Insurance Act 2003 and other sister legislations and the Commission intends to enforce these products. They are

a. Group life Insurance in line with the Pencom Act 2004
b. Employers liability in line with the Workmen's Compensation Act 1987
c. Buildings under construction-section 64 of the Insurance Act 2003
d. Occupiers liability insurance –section 65 of the Insurance Act 2003
e. Motor Third party Insurance –section 68of the Insurance Act 2003
f. Health care Professional indemnity insurance-under section 45 of the NHIS Act 1999

(B) SANITIZATION AND MODERNIZATION OF INSURANCE AGENCY SYSTEM

The introduction of the Network Agency System which would expand the insurance penetration and provide employment to thousands of Nigerians..

(C) WIPING-OUT OF FAKE INSURANCE INSTITUTIONS

The setting up of enforcement teams in all the 36 states of the federation to monitor compliance with the compulsory insurances. The teams would comprise of the Police, VIO, FRSC, Fire Service, Planning

authorities,CORBON,NIA,NCRIB etc.The teams have been constituted and are ready to take off.

(D) INTRODUCTION OF RISK-BASED SUPERVISION

The movement from compliance based supervision to risk based supervision is the way to go in order to reduce stress and distress from the system.

It is believed that if the above issues are properly addressed it will go a long way to resolve all challenges confronting the operations of insurance companies in Nigeria.

4.3 POST CONSOLIDATION CHALLENGES FACING INSURANCE COMPANIES.

Consolidation was done in order to enable Insurance Industries have stronger financial capacity to undertake bigger ticket transactions. But some of the major problems lingering the industry is that of premium collection..More than 80 % of the premium earned in the industry came through brokers.Most of these agents do not give full remittance to the Insurance Companies.

Furthermore, the problem of rate cutting(charging very low) is another issue of concern. In Nigeria, however, insurance companies have often times charged ridiculously low premiums in their efforts to secure businesses, and this reduces their ability to pay claims when losses occur. Most often times, a substantial percentage of the premium on policies were given away in order to secure businesses, while other underwriting costs were incurred, bringing the remaining amount left to the insurers to just about 10 per cent of the premium paid.

This unfortunate situation turn insurance companies into perpetual seekers of new capital at the expense of shareholders even when it may not be easy to raise such capital.

Though experts however pointed out that the premium charged by insurance companies could not be fixed because rates were in the form of a

vicious circle. ”Rates, worldwide, go on a circle; they go up and come down that the rates charged in Africa and other parts of the world depended on the state of the economy and the volume of losses that had occurred.

”When the economy is good and there are few losses, the rates tend to go down because insurers can pay for the losses from their main income but if the economy is down with more losses, insurers may not make much money from investments and will record some losses, which tends to hike the premium rates charged.

The above problems if not solved reduce the underwriter‘s financial ability since there will be less cash to hold in reserve for claims payment or for investment thus this is the reason some members of the public think the companies are inefficient.

Non Presence of Insurance Companies in Rural areas.-Insurance companies and businesses are been not expanded to rural communities. Most of the rural dwellers are not aware of the need of insurance. In the same vain another challenge is the manpower. Most of the Insurance companies do have skilled manpower to manage fund been generated and ICT since consolidation of Insurance companies is to encourage e-insurance.

Political instability and the crisis in the Niger Delta including some other part of the country is serving as a threat for Insurance Industry to reap the full dividends of consolidation.

Religious factor: Most of Nigerians are religiously inclined and they see no need for Insurance for their firm believe in God in whatever happen to their lives and properties.Also conventional insurance as is been practiced today is regarded forbidden in Islam because it contains elements of interests(usury),gambling and uncertainty.In addition there is misconceptions among the muslims about the rationale for insurance in which they see all risk protection (insurance) as haram.(forbidden).

4.4 PRESENTATION OF RESULTS

Table 4.1 presents the regression results of an evaluation of the impact of consolidation of the Insurance companies on the economic growth in Nigeria.The regression estimates were done at 5 percent level of

significance.Data were collected from the annual statiscal bulletin of the CBN, Annual abstracts of statistics from National Bureau of statistics and the Annual reports of National Insurance Commission.

Table 4.1: Regression results

S/N	Variable	Coefficient (t-statistics) Standard Error
	Constant	(28.392)
1	Log GDP	0.041 (0.337) 0.1217
2.	Log Ind	0.357 (2.933) 0.1217
3	Con	0.550 (6.314) 0.0871
4	Log K	0.167 (1.550) 0.1077
5	Log L	0.293 (3.192) 0.0918
6	Doo	0.059 (0.895) 0.0659

Note: $R^2 = 0.952$, $R^{-2} = 0.932$, $F = 46.683$, $DW = 2.273$

Source: Own computation using SPSS Version 13.0

4.5 DISCUSSION OF THE RESULT

The identified relationship between the impact of consolidation of the insurance companies on the economic growth can be investigated by specifying that the growth of the economy (represented by the GDP) is

influenced by the various components of the insurance activities which are captured by the existing operations of the risk analysis. While such relations are proxied by the variables under considerations, it is recognized that the impact of consolidation policy on insurance companies to achieve the desired economic growth may not be necessary contemporaneous, but long lived if properly managed-especially as capital projects and human activities tends to have long gestation periods. Hence the values of capital and labour enters into the model contemporaneously.

The length and significance of these values as captured in the model are so important for two reasons. First, these variables measures the partial effects of the consolidation policy on the growth of the economy, and consequently provides a fertile ground for making judgments as to whether the consolidation exercise have been consistent with the tenets of economic policy making. Secondly as regards the capital and labour as well as the degree of openness of the economy to the outside world which are captured in the model formulation, these variables give a good estimation by using annual data from 1988-2008.These considerations led to the specification of the model as contained in this equation i.e eqn (16) of chapter three.

$$RGDP = B_o + \beta_1 \log Prem + \beta_2 \log Ind + \beta_3 \log Con + \beta_4 \log K + \beta_5 \log L + \beta_6 Doo + U_t$$

This regression equation was estimated using the ordinary least square technique computed from the SSPS version 13.0 software programme. Taking this specification into consideration, the characteristics of the time-series data used for estimating the model were examined apriori in order to avoid the incidence of spurious regression which results from the regression of two or more non – stationary series.The purpose is to give a robust,non parametric findings that can be used for policy analysis.

The result presented in table 4.1 provides an overwhelming evidence that an evaluation of the impact of the consolidation policy of the insurance companies on economic growth can be meaningful if the prevailing economic realities are put into consideration. The model has a very good fit as the coefficient of determination (R^2) explains over 95% of the total

variations in GDP and it's error term are explained by the regressors. From the results, all the variables are positively signed and significant at 95% level.In this result the proxy for insurance policy (consolidation) as dummied is correctly signed and significant and it shows that more than 55 percent variation in insurance policy accounts for a unit change in the growth of the GDP.

To put it more succinctly, the Gross Domestic Product (GDP) of the economy would increase by about 55 percent variation for a unit change in the consolidation policy while holding other economic variables constant. This is an indication that the Nigerian economy has an extremely weak productive base occasioned by poor implementation and policy inconsistency.

The implication here is that in absence of current investment in both physical and human capital,the economy does not have it's own impetus to support growth. Previous efforts to invest in capital and labour did not seem to enhance productivity to support future growth. This indicates that growth in the economy is largely contemporaneous with the effects of it's basic determinants.

Thus,for effective evaluation of the impact of consolidation policy of insurance companies on the economic growth,one would require a consistent planning and policy implementation strategy. The current system of "step-go" policy implementation (possibly occasioned by regime change) is quite inimical to growth. Consequently, the country needs a long term plan to allow for effective gestation period for the actualization of economic growth trajectories.

Next, to this policy of consolidation, the coefficient of indemnity as shown in the result explained that about 36 percent variation in the maximum amount payable by an insurer to a beneficiary of loss is needed for a unit change in the economy's output while holding other variables constant. This is particularly relevant because an insured individual has the capacity and zeal to take an extra risk towards the growth of the economy.

Consolidation policy objectives can be achieved by adjusting the macroeconomic fundamentals inherent in the policy formulation .Indemnifying an individual will entail that the insured pay adequate premium to cover the claims that can satisfy the insurable interest. This study, however is not advocating for high premium payment before an individual could maximally benefit from insurance cover, it is simply saying that more robust policies are needed in the insurance market if the desired growth of the economy is to be realized. It is in this context that the adjusted R- squared (R^{-2}) explains about 93 percent variation in the policy environment which is necessary to adjust the economy in the right direction.

The contribution to the GDP by insurance companies can be gauged through the market portfolio held by insurance companies. Generally, the market portfolio is defined as a portfolio that is made up of all assets in the economy which are held in accordance with their market value weights. This Market portfolio can be represented as a solution to an optimization problem whose analysis may result in the equilibrium (optimality) conditions of the capital asset pricing method relationships.

Consolidating the Nigerian Insurance companies can be evaluated and implemented by adjusting all macroeconomic fundamentals: inflation, exchange rate, and interest rates to give room to mild regulatory conditions that are capable of ensuring that efficient portfolio holdings could lead a class of linear risk sharing between policy holders and the capital markets. In order to cover the total insurance risks involved, the company concerned has to receive enough amount of premium from policy holders and invest such an amount in a risk free assets. In this way, shareholders can be able to offset any investment policy of the insurance company by its investment decision.

When the shareholders themselves can borrow and lend claims at risk- free rate, and are fully liable for losses of the insurance company ,it will make the share of the insurance company to be a combination of a risk-free investment and a short position in insurance contracts.

4.6TEST OF HYPOTHESIS

Since the focus of this study is to identify the appropriate policy direction that could ensure that consolidation in the Insurance companies do have significant impact on economic growth, the model for the study would be evaluated based on the hypothesis that:

Ho: $\beta_1 = \beta_2 = \beta_3 = \beta_4 = \beta_5 = \beta_6 = 0$

Against

Hi: $\beta_1 \neq \beta_2 \neq \beta_3 \neq \beta_4 \neq \beta_5 \neq \beta_6 \neq 0$, implying that not all β's are zero

At 95 percent.

This is achieved by testing the F-statistics[1].From the result,the computed F (i.e F*) IS 46.683 while the tabulated F(i.e F_T) with K- 1,N-K degrees of freedom at 5 percent level is 2.85.The value of F* is absolutely greater than the value of F_T. Consequently,the null hypothesis is rejected because the regression is significant with the implication that not all the parameters estimates are zero at 95 percent level. This scenario leads credence to the fact that consolidation policy may have positive impact on the economic growth of the country if all structural bottlenecks to implementation are removed.

4. 7 POLICY ISSUES OF THE FINDINGS:

The findings of this study seems to suggest that financial sector reforms-particularly those of the insurance companies in Nigeria would be yielding positive results if adequate macroeconomic fundamentals are adjusted to reflect the current circumstances. Some of the policy implications of these findings are that there is the need to ensure normalization of interest rates, exchange rates, and the general price level whose variations should not be such that could discourage the consolidation exercise.

The success of any consolidation exercise depends more fundamentally on three main factors:

(a) Political commitment,

(b) Logistical frame work and

(c) Creating the enabling environment.

This is because, experience have shown that no reform in the financial market can succeed under a vague political commitment while the capacity to carry out such reform rests on the underlying regulatory frame work and the competence of those entrusted with its implementation.

Finally, creating enabling environment are necessary to enhance consolidation because all financial reforms involves difficult decisions regarding the costs of credits, inefficiency of some financial institutions and the removal of distortions in the overall market environment.

END NOTES.

1 $F^* = \frac{\sum Y2/(K-1)}{\sum e2/(N-k)}$

$F_T = \frac{R2/(K-1)}{(1-R2)/(N-K)}$

CHAPTER FIVE

SUMMARY, RECOMMENDATIONS AND CONCLUSIONS

5.1 SUMMARY

This study has attempted an evaluation of the Nigerian Insurance companies consolidation within the theory of corporate finance. The consolidation exercise embarked upon was against the background of excessively weak regulations that characterized the insurance industry. The study found that the insurance industry consolidation exercise embarked upon before the 2005 policy was not followed by a remarkable improvement in the strength and vibrancy of the insurance sub sector of the economy and that such consolidation policies were unaccompanied by adequate insurance coverage to all Nigerians. The inability of the Insurance sub sector reforms to meet the desired objectives were due largely to many structural factors such as macroeconomic instabilities of all magnitude alongside political will and inadequate enabling environment that constrained the policy thrust of the reforms.

The main area in which consolidation is important are; maintaining a sound macroeconomic fundamentals such as low and stable prices, fiscal balances and liberalizing the external sector through exchange rate stability.

5.2 RECOMMENDATION

The recommendations is divided into specific and general. The specific policy implications and recommendations from the findings are that there should be:

(a) Review, update and implement all existing provisions in the relevant laws and regulations that govern the operations of the insurance industries to ensure high level professionalism and probity of owners, operators and regulators of the insurance companies.

(b) Incentives should be provided to promote and support specialized institutions and agencies to facilitate easy access to insurance coverage. Those industries that specialized in either life or Non-life should be capable of discharging their functions without hiccups.

((c) Islamic takaful (insurance) practice should be encouraged in Nigeria to provide diversification in the Insurance sector for better economic growth.

The general recommendations are:

IMPROVED PRODUCT OFFERINGS

The Insurance practitioners must deliberately strive to identify the needs of their consumers, plan products that will adequately meet those needs, properly price, promote and distribute those products such that both parties will mutually benefit from the process. In other words, the insurer must translate not only the customers' needs into product and service requirements but also must deliver the products at competitive rates with the right quality. Insurers should therefore not underestimate the importance of product features and strategy even as they pursue their distribution networks after consolidation. Takaful (Islamic Insurance) is significant in the need to innovate as conditions change and to service unmet demands or segments. There should be an Insurance industry with adequate capacity and expertise to manage complex business transactions as they emerge in this increasingly globalised world. In other words, in post consolidation, we need an insurance industry whose product portfolio allows the insurers to serve as many target .customers as possible while responding quickly to the changing needs of the market. To achieve this
status, the product offerings must be aligned with the insurer's broad value proposition and strategic direction.

CHARGING ADEQUATE PREMIUM.

The focus of the insurance industry in post consolidation should be towards ensuring that companies charge adequate premium that is commensurate with the risk they are insuring.
The regulatory authorities must also come together to fashion a way forward in this regard in the overall interest of the insurance industry in

Nigeria. The Insurance Industry must be able to speak with one voice for once on a crucial matter of common interest that is capable of destroying the insurance industry. It is envisaged that with market-induced consolidation and mergers of insurance companies, companies will be able to more work together as a team towards charging adequate premium that will be commensurate with the risk Insurance companies are carrying.

AGGRESSIVE CAMPAIGN TO MAKE PURCHASE OF INSURANCE POLICY A VOLUNTARY ACT

Many players desire a situation where the purchase of insurance is driven by conviction of its value rather than in compliance with regulatory requirements. This is because, if certain insurance policies were not mandatory, many policyholders would not have procured them! As some have come to realise, only the occurrence of disaster drives home the inevitability of insurance as mechanism for reducing losses or mitigating the effects of disasters. Indeed, prior to now, only the motor insurance was statutorily
compulsory. With the recent Pensions Reform Act, the Building Act, the National Insurance Act, etc, the list has lengthened. We sincerely believe that if the citizenry appreciate the importance of insurance, they will not wait for the law to make it compulsory or for disaster to occur before procuring policies. In post consolidation,
there should be an aggressive marketing of insurance both by regulators and insurers to enlighten the populace of the importance of insurance in the consummation of business. The Insurance Institute must also play a key role in this awareness crusade whose thrust should include the simplification of the language of insurance policies, penetration into rural markets and elimination of hidden clauses. Without doubts, winning the confidence of the insured is crucial. Confidence can only be built if the insured understands what he/she is being encouraged to purchase.

GREATER PREMIUM ON HUMAN CAPITAL DEVELOPMENT

It is generally accepted that the most important asset of any organization is its people. They make things happen. They are the soul and controlling mind of the organization. Indeed, Lord Justice Denning (as he then was) opined persuasively in a case in 1957, that the controlling minds of a corporation would naturally be its directors or superior officers. The state of mind of

these people is the state of mind of the company. By implication, the quality of the leadership of the insurance companies will inevitably define its position on the ladder of success. Selecting the right leadership and personnel from the outset is a precondition for placing the ladder of success on the right wall. Training the personnel hired on a regular basis will ensure that the company climbs the ladder of success effortlessly . It is in this respect that we desire a market with the right skills such that the market will be a safe, strong and responsive insurance industry able to meet the challenges of modern day business. We must start early to lay the solid foundation if we sincerely desire to be the first choice insurance market in Africa and the 20th best market in the world by the Year 2020.

ADOPTION OF ICT-DRIVEN FOR INSURANCE COMPANIES

In post consolidation, the Industry should adopt high information technology (IT)-driven and financially resilient strategies to be able to deliver on their promises such that the sector will ultimately occupy its rightful place in economic activities in Nigeria. The industry will be able to redeem its waning image through prompt settlement of verified claims. Indeed, many operators in the industry have come to realize that verification of claims can be expeditiously done through the adoption of appropriate software and the creation of a single customer data-base from disparate back-office systems including underwriting, claims, billing, policy-management, etc. With increased re-capitalisation and market-driven mergers, it is hoped that many insurers would be able to create a single source of customer data using information technology (ICT) facilities such that a single, real-time view of customers' total portfolio will be available to agents, brokers and sales executives.

ESTABLISHMENT OF MICRO-INSURANCE

As part of its efforts to empower more Nigerians, the government through the Central Bank of Nigeria, has licensed some MicroFinance Banks that are currently providing credit facilities to players in the informal sector. Micro Insurance companies should be established to explore a lot of business opportunities in this sector (informal) as they can provide insurance cover to these small investors at very small rates. This will

encourage these budding entrepreneurs and their financiers to take more informed risks which will increase activities in these untapped but potentially viable sector of the economy

REGULATION

The oversight functions of the regulatory authorities should expand to include the verification of the exact worth of shareholders' funds of insurers in the market. It is imperative that the capacity of the insurer to underwrite policies is unimpaired by losses and sharp practices of persons in governance responsibilities. Secondly, given the growing spate of receivables in the industry, it should be easy to appreciate the need for the regulatory authorities to regularly visit insurance Companies and Insurance brokers to ensure compliance to the rule on remittance of premiums. The full weight of the law should be brought to bear on deviants as a deterrent to others.

The regulators should encourage insurance companies to strengthen their credit control departments with appropriate and aggressive professionals who can effectively track and collect receivables from intermediaries. Furthermore, investment in Information technology (IT) will also assist Insurance companies in having error free statement of account. In keeping with the imperative to pursue sustainable growth, there is need to improve the internal controls of insurance companies not only to eliminate wastes and improve their efficiency but also to ensure that business decisions are optimally taken. In this respect, they must constantly review their value chain in order to achieve the desired level of performance. Indeed, improved performance is the whole essence of re-engineering. As risk managers, insurers must know their risks, how to control those risks and manage business lines such that ultimately, the business people have responsibility for risk management

When these recommendations are put in place, they would enable the Nigerian economy to realistically gain more from the contributions of the insurance sub –sector.

5.3 CONCLUSION

The continued "step-go" system of implementing policies in Nigeria-particularly as they concern the Insurance industries proves the case for inconsistency in policy formulation and implementation.

In view of the lessons from the present global and economic realities, if the intermediate and long-term economic aspirations to make Nigeria among the 20th most industrialized countries of the world(FSS 2020) , efforts should be directed to develop a modern, well-structured, efficient and competitive insurance sub sector that caters for the long term needs of the economy.

This can be achieved by creating a risk management instruments and products that are customize to the peculiarities of various areas of economic endeavor for overall economic activities that may not have been given priorities otherwise.

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APPENDIX I

RAW DATA FOR REGRESSION

GDP (Million)	Premium (000)	Indemnity (000)	Consolidation	Capital	Labour	Oper
219,875.6	506,675.0	357,548.0	0	17,562.21	287,533	0.353
236,729.6	701,764.0	577,380.0	0	26,825.51	279,550	0.603
267,550.0	1,048,443.0	698,531.0	0	40,121.31	287,533	0.530
265,379.1	1,334,237.0	957,774.0	0	45,190.23	183,254	0.648
271,365.5	2,517,901.0	2,482,515.0	0	70,809.16	191,329	0.610
274,833.3	5,901,257.0	5,975,734.0	0	96,915.51	197,071	0.580
275,450.6	14,671,675.0	3,798,880.0	0	105,575.49	200,137	0.423
281,407.4	14,587,649.0	5,365,060.0	0	141,920.24	200,018	0.597
293,745.4	13,150,563.0	5,916,139.0	0	204,047.61	197,211	0.576
302,022.5	16,519,018.0	6,499,399.0	0	242,899.79	198,087	0.768
310,890.1	17,846,471.0	7,174,281.0	0	242,256.26	199,287	0.661
312,183.5	10,879,630.0	5,923,180.0	0	231,661.69	3659,203	0.558
329,176.7	14,047,520.0	5,629,520.0	0	331,056.73	3,539,891	0.713
356,994.3	18,440,700.0	6,110,520.0	0	372,135.65	4,079,381	0.818
433,203.5	21,927,620.0	7,839,710.0	0	499,681.53	4,019,156	0.633
477,533.0	36,807,670.0	9,415,210.0	1	865,876.46	4,244,968	0.752
527,576.0	41,431,150.0	12,084,030.0	1	863,072.62	4,354,617	0.484
561,931.4	50,348,270.0	12,402,400.0	1	804,400.82	4,523,792	0.501
595,821.6	13,422,350.0	12,774,472.0	1	1,546,525.65	4,244,968	0.674
634,251.1	16,274,390.0	13,157,706.0	1	78,981.31	4,244,968	0.651
674,889.0	16,762,621.0	13,552,437.0	1	73,606.48	4,354,617	0.646

Source:Statiscal Bulletin of CBN,Annual abstracts of Statistics of NBS,Annual reports of NAICOM

APPENDIX II

Regression Data

Year	Log of Real GDP	Log of Premium	Log of Indemnity	Consolidation	Log of Capital	Log of Labour	Degree
1988	5.34	5.71	5.55	0	4.2450	5.46	
1989	5.37	5.85	5.57	0	4.4290	5.45	
1990	5.43	6.02	5.84	0	4.6030	5.46	
1991	5.42	6.13	5.98	0	4.6550	5.26	

1992	5.43	6.40	6.39	0	4.8500	5.28	
1993	5.44	5.77	6.78	0	4.9860	5.30	
1994	5.44	7.17	6.58	0	5.0240	5.30	
1995	5.45	7.16	6.73	0	5.1520	5.30	
1996	5.47	7.12	6.77	0	5.3100	5.29	
1997	5.48	7.22	6.81	0	5.3850	5.30	
1998	5.49	7.25	6.86	0	5.3840	5.30	
1999	5.49	7.04	6.77	0	5.3650	6.56	
2000	5.52	7.16	6.75	0	5.5200	6.55	
2001	5.55	7.27	6.79	0	5.5710	6.61	
2002	5.64	7.34	6.89	0	5.6990	6.60	
2003	5.68	7.57	6.97	1	5.9370	6.63	
2004	5.72	7.62	7.08	1	5.9360	6.64	
2005	5.75	7.70	7.09	1	5.9050	6.66	
2006	5.78	7.13	7.11	1	6.1890	6.63	
2007	5.80	7.21	7.12	1	4.8980	6.63	
2008	5.83	7.22	7.13	1	4.8670	6.64	

APPENDIX III

Variables Entered/Removed(b)

Model	Variables Entered	Variables Removed	Method
1	Degree of Openness, Consolidation, Log of Capital, Log of Labour, Log of Premium, Log of Indemnity(a)	.	Enter

a All requested variables entered.

b Dependent Variable: Log of Real GDP

Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics					Durbin-Watson
					R Square Change	F Change	df1	df2	Sig. F Change	
1	.976[a]	.952	.932	.03970	.952	46.683	6	14	.000	2.273

a. Predictors: (Constant), Degree of Openness, Consolidation, Log of Capital, Log of Labour, Log of Premium, Log of Indemnity

b. Dependent Variable: Log of Real GDP

ANOVA[b]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.441	6	.074	46.683	.000[a]
	Residual	.022	14	.002		
	Total	.463	20			

a. Predictors: (Constant), Degree of Openness, Consolidation, Log of Capital, Log of Labour, Log of Premium, Log of Indemnity

b. Dependent Variable: Log of Real GDP

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	4.497	.158		28.392	.000
	Log of Premium	.010	.029	.041	.337	.741
	Log of Indemnity	.110	.037	.357	2.933	.011
	Consolidation	.181	.029	.550	6.314	.000
	Log of Capital	.048	.031	.167	1.550	.143
	Log of Labour	.068	.021	.293	3.192	.007
	Degree of Openness	.080	.090	.059	.895	.386

a. Dependent Variable: Log of Real GDP

Residuals Statistics[a]

	Minimum	Maximum	Mean	Std. Deviation	N
Predicted Value	5.3588	5.8014	5.5486	.14856	21
Residual	-.06415	.08760	.00000	.03321	21
Std. Predicted Value	-1.277	1.702	.000	1.000	21
Std. Residual	-1.616	2.207	.000	.837	21

a. Dependent Variable: Log of Real GDP