THE IMPACT OF COOPERATION BETWEEN INSURERS AND BANKS ON THE DEVELOPMENT OF THE INSURANCE SYSTEM

Nataliya PRIKAZYUK[1], Ganna OLIYNIK[2]
Taras Shevchenko National University of Kyiv, Ukraine

Abstract. The article highlights how the cooperation of insurance companies and banks affects the insurance system. Defined the concept of bancassurance, provided a brief description of the main bancassurance models in the context of their impact on the insurance system. Defined the main benefits and risks that accompany cooperation of insurance companies and banks within different models of association. It is noted that despite the generally accepted benefits of cooperation between insurers and banks, financial intermediaries' unions often carry significant risks. Benefits from the cooperation of insurance companies and banks are disclosed with operational, marketing and financial aspects. *The purpose* of the article is to study the forms of cooperation between financial intermediaries and their impact on the insurance system. *Methodology*. The study is based on theoretical methods to study this problem. The theoretical and methodological basis of the study is works of scientists on the models of cooperation between insurers and banks. The dialectical method of cognition as well as such methods as logical generalization, structural and systematic analysis are used to study the methodological foundations of banks' impact on the insurance companies and insurance system. *Results*. Banking activity has a significant impact on the insurance system. This impact is noticeable at the micro-level: insurers and banks can be clients of each other as well as they can sign cooperation agreements. A significant positive impact of the bancassurance on the activities of both financial institutions within the synergy that appears during their cooperation is highlighted in the article. Respectively, the insurance company and the bank are experiencing the benefits of cooperation along with savings on fixed, variable costs and obtaining additional profits; simplifying and optimization of the process of collecting and processing information; savings on advertising and marketing research. *Value/originality*. Despite the numerous works on this subject, such an issue like the impact of insurers and banks cooperation on the insurance system development remain insufficiently studied. The article highlights the impact of the banking system on insurance as from the perspective of their interaction and the factors of direct and indirect influence of banking activities on the insurance system.

Key words: bank, insurance company, bancassurance, cooperation, financial intermediaries.

JEL Classification: G21, G22, G34

1. Introduction

The activities of insurance companies and banks are historically related. Insurers and banks significantly affect each other as active members of a single financial system. Moreover, the impact of banking on all of the systems of the financial market, including insurance, is considered to be the most noticeable. It can be explained by the fact that the banking sector is the most powerful and its share of the financial market is the largest. Therefore, its fluctuations significantly influence the activities of other market participants. The influence of banking on insurance system can be considered at two levels: micro-level – banks' impact on insurance companies within their joint activities and macro-level – the state level.

Collaboration and cooperation of financial intermediaries in providing financial services become one of the main characteristics of modern economic space. Such cooperation is gaining increasingly larger scales. It becomes a common phenomenon and provides new prospects for the development of the financial system and its separate subsystems. The cooperation of insurance companies and banks is the most common occurrence, despite the great number of financial institutions. Historically, the banking and insurance activities are closely related, therefore, their

Corresponding author:
[1] Department of Insurance, Banking and Risk Management, Taras Shevchenko National University of Kyiv.
E-mail: pnvuniv15@ukr.net
[2] Department of Insurance, Banking and Risk Management, Taras Shevchenko National University of Kyiv.
E-mail: oliynik_anna@ukr.net

partnership is not accidental. It's economically justified for both parties.

2. The main aspects and models of cooperation

It should be noted that insurance companies are interacting with banks constantly while conducting their activities. This interaction starts with the maintenance of insurer's monetary circulation by the bank and ends with higher forms of cooperation.

The main aspects of insurance companies and banks interaction are presented in Figure 1.

Thus, the relationship between the bank and the insurance company is formed at different levels and in different fields. Most often the cooperation between insurers and banks is called bancassurance.

In our opinion, in the broad sense, bancassurance is a legally executed agreement between the bank and the insurance company to meet the needs of consumers in insurance (banking services) through the bank (insurance) distribution channels.

The degree of interaction between banks and insurance companies greatly influences the activity of insurance companies and insurance system in general. So we consider it necessary to disclose the different models of cooperation between banks and insurance companies, describing the main features they offer and the risks they carry.

Primarily, insurance companies and banks are customers of each other. Bank performs cash management services of the insurance company; accepts deposits from insurance companies; may be its lender.

So, the first step of interaction between banks and insurance companies is the stage of mutual services, as the quality of services could influence the choice of the partner for cooperation.

The agency agreement is the initial stage of cooperation between the insurance company and the bank, financial intermediaries are responsible solely for services rendered (thus securing themselves from a number of risks), and financial results of such cooperation are relatively small.

More integrated forms of cooperation between insurers and banks proved its effectiveness in the world. Complex and interconnected structure provide a substantial interest of the parties to achieve common goals and, therefore, greater responsibility for joint activities and reputation of each other. However, complex structures not only could lead to additional benefits of financial intermediaries but also entails additional risks. Selecting the appropriate models of cooperation should depend on the overall economic and political situation in the country, the state of the financial services market and objectives to be set by the financial intermediaries.

The strategic alliance between the bank and the insurer is the next-stage model of cooperation after the agency contract. At this stage, insurance companies and banks do not have shares in the capital of each other, but the intention of cooperation is greater than when signing the agreement and the customer base of the insurer and the bank at this stage tend to unite. The main advantage of the strategic alliance is that the insurer and the bank do not take additional risks, are completely independent of each other in the financial and organizational aspects (Charles, Vincent, Huldah 2004).

Creation of a joint venture (bank insurer) requires the additional funding of banks and insurance companies. Typically, one of the transaction participants is the moderator (makes a larger share of the joint venture) and, therefore, has a greater influence in decision-

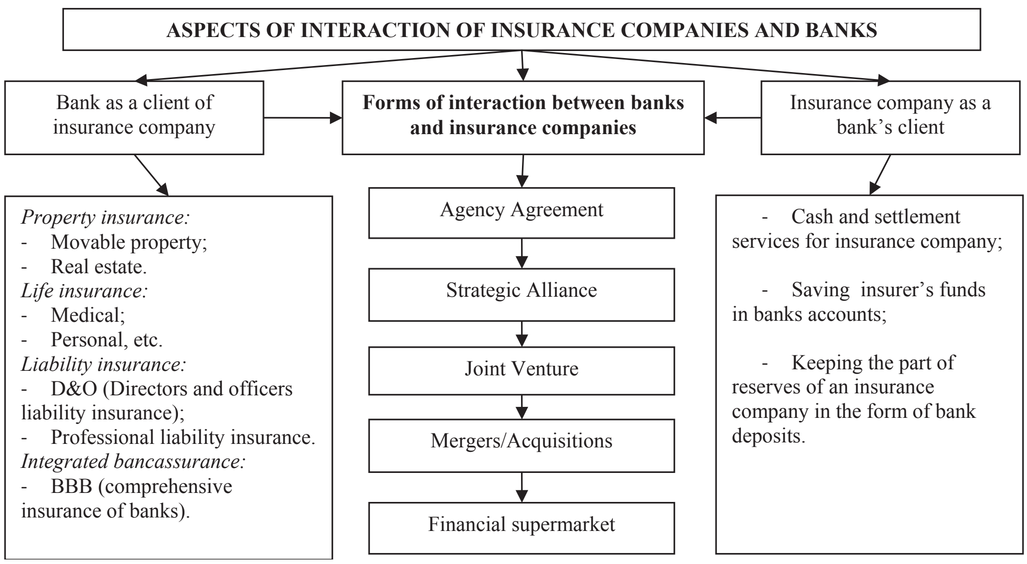

Fig. 1. Aspects of interaction of insurance companies and banks

Source: compiled by the author, based on (Prikazyuk, 2008) making and gets a higher revenue. The advantage of this interaction is a clear separation of the insurance and banking: each financial intermediaries dealing with the exclusively own profession. Common features of the insurer and the bank shifted to the newly created company (Szewieczek, 2013).

The next model of interaction between banks and insurance companies is mergers/acquisitions. For banks, mergers/acquisitions have several advantages. Compared with the foundation of its own insurance company, the process of mergers and acquisitions for the bank is easier and takes less time. Primarily, the bank does not have the internal capacity to insurance processes, so it strives to find insurers that have a positive reputation in the market, developed infrastructure, highly qualified staff, and a stable customer base.

However, mergers and acquisitions between insurers and banks are less common than the full union of several financial intermediaries because it requires a complete transfer of assets from an insurer to a bank (if the bank initiated mergers / acquisitions). This operation entails major risks: firstly significant investment may not bring the expected profits in the future, and secondly, changing the legislative requirements and regulations for insurance companies and joint activities may lead to loss of a bank.

The financial supermarket is a highest and quite common model of financial intermediaries' cooperation that provides customers the possibility to get banking and insurance services, buying and selling shares and bonds, mortgages and more. Often comprehensive financial services are carried out online. In times of ever-increasing pace of life and constant lack of time, financial supermarket concept is particularly relevant (Martin, Rey 2001).

Often the benefits of bancassurance are mentioned in the literature but there is also the negative impact of insurers' and banks' joint activities:

- Reduction of loyalty to the tandem of financial institutions because of disloyalty to one of the partners;
- Reducing the number of customers as a result of the imposition of insurer bank's partner;
- Restricting range of insurance services to those in which the bank is interested;
- Reduced income of insurers due to overloading by bank's commission for mediation services.

It should be noted that the decision to cooperate is accepted by the senior management of financial institutions; selling of financial services via the bancassurance channel is carried out through the front offices of the companies; collection, processing, and analysis of information is exercised through the back offices.

One should take into consideration that both financial institutions have to reach agreement on certain organizational, financial, and management issues for conducting joint activities.

Models, methods of implementation and main characteristics of bancassurance can vary depending on the country and on conditions, in which it occurs.

It is also important to take into consideration what kind of bank and insurance company will conclude an agreement on bancassurance.

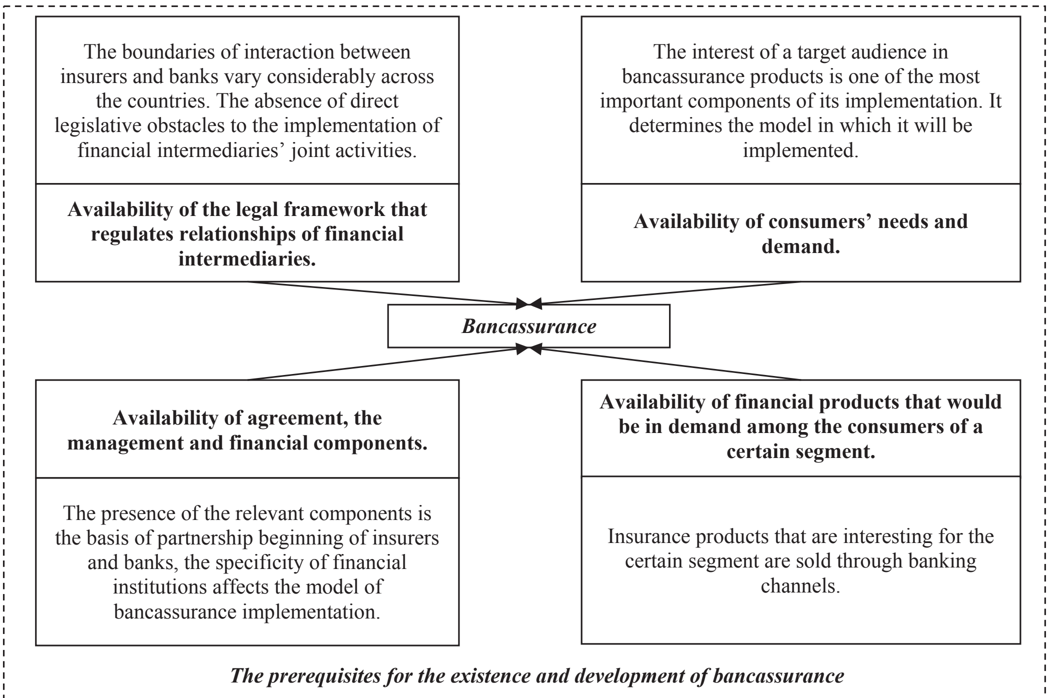

Fig.2. The prerequisites for the existence and development of bancassurance

Source: compiled by the authors

These factors affect the bancassurance forms and they are crucial in its organization. The prerequisites for the existence and development of bancassurance are presented in Figure 2.

In general, the implementation of bancassurance has a significant positive impact on the insurance company as well as on the bank. This effect, as a rule, leads to the development of both institutions. Consequently, the development of insurance companies positively affects the development of the entire insurance system.

Positive trends from the implementation of bancassurance are embodied in the following aspects: financial, operational, and marketing aspect (Fig. 3).

The financial aspect is realized through a larger profit that the financial institutions can get. It means that the number of financial services that are sold by the bank and the insurance company increases but, at the same time, overall costs are reduced or remain unchanged. For example, fixed costs for salaries, rent, utilities remain the same because the bancassurance products are sold through banking channels and don't require the lease of new premises or attracting new employees. It can be carried out by a representative of the insurance company, who is located in a bank branch or by the bank employee who was specially trained. Also, the costs for hardware and software can be included to the fixed costs. The development of new software is essential when creating a new company (bank insurer). If the bancassurance is implemented through banking distribution channels, the software development and purchase of new computer equipment are optional.

Insurance costs and costs for new customers' attraction belong to variable costs. Insurance costs are reduced because the bank as a partner of the insurance company uses certain preferences (discounts) for personal property insurance and employee insurance. Also, when conducting the joint activities, the insurance companies and banks often have an access to the customer bases of each other, which significantly reduces the costs of financial institutions to expand customer bases.

Operational aspect of the implementation of bancassurance is embodied by simplifying the technological processes, which are associated with the processing and analysis of financial information. Access to the partner's technologies and the achievements is another element of the operational aspect of cooperation between insurers and banks. The reduction of technological processes that accompany the search for new customers can be also considered as a result of the merger of two customer bases.

The marketing aspect is embodied by the improvements in the development of the new financial product. Since the development and implementation of new financial products, as well as market research for new products in the financial services market, are characterized by a fairly high cost, the attractiveness of the cooperation between insurance companies and banks grows even greater.

Also, the marketing effectiveness of two financial institutions increases thanks to the ability to reach a larger segment of the market (the insurance company's clients automatically become clients of the bank) and thanks to geographical diversification. In addition, the cooperation between insurers and banks has a positive impact on the reputation of both financial institutions. Cooperating with the insurance company the bank gets additional benefits by increasing its own sales volume due to the fact that the banking products that include an insurance component give the customers a greater confidence in them.

Each of the aspects listed above is fully realized by synergy that accompanies any process of institutions' merger or their separate elements. Synergy implies the achievement of a greater effect as a result of joint activities of financial institutions than when the bank and the insurance company operate separately.

In these aspects, synergy appears in the following ways:

- In the financial aspect, additional profits appear beside the saving of fixed and variable costs. The insurer significantly increases the number of channels, and thus the volume of sold insurance products increases. Bank profits rise due to commissions that are received from insurers.

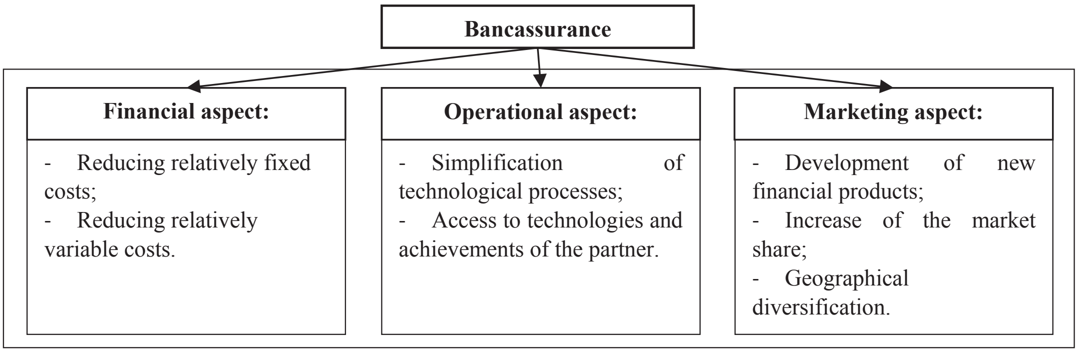

Fig. 3. Aspects of bancassurance implementation

Source: compiled by the author, based on (Szewieczek, 2013)

- In the operational aspect, the synergy effect is more visible at the level of back-offices of the insurance company and the bank, as the collection, analysis, and processing of information that is necessary for the financial institutions' activities are carried out at this level. Banks and insurance company are able to distribute the costs for the salary of back office staff, their hardware, and software.
- In the context of the marketing aspect, the synergy is embodied in the form of savings on marketing campaigns (advertising) and marketing research. This occurs due to cost allocation between financial intermediaries and thanks to the fact that marketing achievements of the insurance company and bank make it possible to achieve a greater effect on the financial services market.

However, the transience and the uncertainty of the development of the global financial system have a permanent effect on all spheres of economic activities, including banks and insurance companies. Thus, the cooperation between banks and insurance companies falls under the double impact of risks: risks of the environment, on the one hand, and the risks of the banking and insurance activities, on the other hand. The difficult economic situation in the domestic financial market complicates the implementation of the partnership of insurers and banks.

Studying the different aspects of cooperation between banks and insurance companies, one cannot determine its impact on the insurance system unambiguously since such cooperation brings both advantages and threats for insurance companies and, therefore, for the entire insurance system.

3. The impact of banks on the insurance system

In general, when analysing the cooperation between insurance companies and banks, one need to focus on the studying of impact, which the banks have on insurers and, consequently, on the entire insurance system.

The banking system is more developed than the insurance industry in the vast majority of countries. As a rule, assets of the banking system substantially outweigh the total assets of insurers. Thus, the stability and the development of the national economy depend largely on the efficient and uninterrupted operation of the banking system. Consequently, the banking system has a significant impact on all segments of the financial system on the whole and on the insurance system in particular.

In our opinion, the impact of banks on insurance companies and insurance system can be divided into managed and unmanaged; also, there are some indirect banking factors that can influence the insurance.

Thus, the factors of influence that depends on banks include the following:

1. Banks' loyalty to insurance companies. Banks and insurance companies may have a different approach to partnership. When concluding agreements on long-term periods, banks and insurance company can strengthen their market position thanks to achieving sustainable competitive advantages as partners. In Ukraine, banks consider insurance companies only for obtaining an additional income. This situation is common today. The insurance company is not considered by the bank as a long-term strategic partner.

However, the experience of developed countries shows that the cooperation between the bank and the insurance company for many years, along with favourable socio-economic conditions, strengthens the position of both financial intermediaries in the market and provides a basis for the qualitative deepening of their partnership.

2. Bank downgrade or bankruptcy. First of all, we should note that the downgrade and, especially, a bankruptcy of a major bank have a significant negative impact on the national economy (the occurrence of so-called systematic risk). Sometimes the bankruptcy of a major bank or financial conglomerate becomes the beginning of the economic crisis. Such cases are not rare in the world practice.

Considering the impact of the downgrade of the bank or its bankruptcy on the activities of insurance companies more detailed, it should be noted that the insurance company as a client of the bank falls under the significant risk of non-repayment of deposits and funds on accounts. If the volume of deposits is substantial, it can significantly harm the solvency and liquidity of the insurance company, by creating additional risks of its activities, and adversely affecting the development of the insurance system, especially if this insurance company is systemically important. Secondly, the downgrade of the bank or its bankruptcy can negatively affect the rating of the insurance company, as a partner of this bank, which threatens the loss of customers.

We believe that the factors that don't depend on banks include the following:

1. State regulation of banking and insurance activities. Government authorities may impose a ban on any agreements between financial intermediaries or set clear boundaries of their interaction. For example, in the first half of the 20th century as a result of the economic crisis in Italy and America, the laws that were restricting the speculative activities of banks (Amato Law and Glass-Steagall Act respectively) were adopted (Broner, Ventura, 2010). Thus, banks were not allowed to be engaged in insurance and securities transactions and, therefore, they lost a source of additional income as a participation in providing the insurance services. Insurance companies, in their turn, lost potential customers and distribution channels of their services. Since banks have significant information, these "missed opportunities" are noticeable for insurance companies.

Establishing of particular limits of interaction between banks and insurance companies at the level of the

Agency Agreement is another example of government restrictions in Ukraine.

2. Since banks occupy the largest share in the financial market, customer loyalty to banks often determines their loyalty/trust in all financial intermediaries, including insurance companies. Regardless of the number of banks in a country, the stable banking system demonstrates the stability of the financial market (the entire country's economy). Therefore, under these conditions, all kinds of financial services (banking, investment, insurance, consulting, etc.) are in constant demand among the population. And conversely, the absence of clients' loyalty to banks, all financial intermediaries (including insurance companies) suffer from a shortfall in revenues.

In our opinion, the indirect impact of banks on insurance companies consists of the following:

1. By increasing the volume of lending banks influence the money supply that may affect the activity of the consumption of insurance services and the level of their prices.
2. Growth in consumer loans and mortgages is causing increased demand for insurance products. By mitigating terms of the mortgage, consumer, and other loans, banks at the same time attract a significant number of new customers to the insurance companies. It is connected with the compulsory insurance of collateral and the borrower's life insurance.
3. The impact of banks on insurance companies can be considered in terms of competition for customers. Clients' funds that can be placed in bank deposits or in the form of investment in long-term life insurance is the basis of competition between banks and insurance companies.

So, in order to attract more customers and, accordingly, a greater volume of temporarily free funds, insurance companies have to offer their customers a higher rate of returns than bank interest. The funds that are attracted by the insurance companies in the form of contributions and by banks in the form of deposits constitute the financial basis of investment activities of financial intermediaries.

Investment activities can be also considered as a competitive basis of financial intermediaries. In the conditions of a limited number of attractive investment projects, banks, and insurance companies have to look for additional investment options.

4. Conclusions

Banks occupy a leading part among other financial intermediaries in most countries and do a significant impact on the entire financial market and the insurance sector in particular. Being a partner of the insurance company, a bank may significantly affect the volume of insurance, profit of insurance companies and customer loyalty to them. This effect may have both positive and negative consequences. At the macro level, the banking sector is able to influence the insurance business directly (managed and unmanaged factors) or indirectly.

The impact of cooperation between insurance companies and banks on the insurance system depends largely on the level of such cooperation, activities of the banks and the government, which controls their activities, as well as on independent factors such as competitive market conditions and changes in lending volumes. Balanced and effective banks' activities and its reasonable control guarantees the stability of the banking system development and has a positive impact on all segments of the financial market, including, insurance system.

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Наталия ПРИКАЗЮК, Анна ОЛЕЙНИК

ВЛИЯНИЕ ВЗАИМОДЕЙСТВИЯ СТРАХОВЫХ КОМПАНИЙ И БАНКОВ НА РАЗВИТИЕ СТРАХОВОЙ СИСТЕМЫ

Аннотация. В статье раскрыто, как сотрудничество страховых компаний и банков влияет на систему страхования. Дано определение банкострахования и краткое описание основных моделей банкострахования в контексте их воздействия на страховую систему. Определены основные преимущества и риски, которые сопровождают сотрудничество страховых компаний и банков в рамках различных моделей банкострахования. Отмечается, что, несмотря на общепринятые преимущества сотрудничества между страховщиками и банками, объединения финансовых посредников часто несет значительные риски. Преимущества сотрудничества страховых компаний и банков раскрыты с позиции операционного, маркетингового и финансового аспектов. *Цель статьи* – изучить формы сотрудничества между финансовыми посредниками и их влияние на систему страхования. *Методология*. Исследование основано на теоретических методах исследования этой проблемы. Теоретической и методологической основой исследования являются труды ученых о моделях сотрудничества между страховщиками и банками. Диалектический метод познания, а также такие методы, как логическое обобщение, структурный и систематический анализ, используются для формирования методологических основ влияния банков на страховые компании и систему страхования. *Результаты*. Банковская деятельность оказывает значительное влияние на страховую систему. Это воздействие заметно на микроуровне: страховщики и банки могут быть клиентами друг друга, а также могут подписывать соглашения о сотрудничестве. В статье подчеркивается существенное положительное влияние банкострахования на деятельность финансовых организаций в рамках синергии, проявляющейся в ходе сотрудничества. Соответственно, страховая компания и банк пользуются преимуществами от сотрудничества благодаря экономии на постоянных и переменных издержках и получении дополнительной прибыли, упрощении и оптимизация процесса сбора и обработки информации, экономия на рекламных и маркетинговых исследованиях. *Новизна*. Несмотря на многочисленные работы по данной тематике, такой вопрос, как влияние сотрудничества страховщиков и банков на развитие страховой системы, остается недостаточно изученным. В статье раскрывается влияние банковской системы на страхование с точки зрения их взаимодействия, а также рассматриваются факторы прямого и непрямого влияния банковской деятельности на страховую систему.