

MAJOR FACTORS INFLUENCING INSURANCE COMPANIES IN THE MIDDLE EAST

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ABSTRACT

The main purpose of this research is to evaluate the major factors that affect the insurance industry in the Middle East countries through applying the principal component analysis method (PCA). The researchers studied and analyzed 19 variables that have an impact on the insurance industry in the Middle East.

These variables were summarized into eight major factors based on their importance, among them the inter-developed insurance culture, and the industry's dependence on traditional insurance products. These variables were categorized according to their significance, and in light of the nature of the implication of every factor.

The study revealed that the first factor "Inter developed insurance culture" was the most significant factor, followed by the second factor "Industry's dependence on traditional insurance products", and then comes the eighth factor "The weakness and strength of the appropriate legislation and regulatory systems that are applied in the Arab countries in terms of legislation, supervision and regulation of the industry".

Keywords: Insurance Industry, Re-Insurance, Factor Analysis.

INTRODUCTION

The process of pooling insurance premiums, the consolidated capital will play an important role in enhancing the development and prosperity of the national economy, as it is a form of regular savings, where insurance companies provide the national economy with the necessary the capital that could be invested in several projects to achieve gains and profits for the community members and contribute in achieving the goals of the economic development. Moreover, insurance plays a significant role in risk prevention and reduces any expected risk by addressing such challenge and discussing their causes.

The insurance companies practice a twofold role in terms of providing insurance service for the customers and collecting money from the insured parties in order to re-invest such amount different projects that create shared returns. Therefore, the development of the insurance industry will become a finance source for investments, and thus improves the GDP in the emerging and developing countries. Therefore, this study will answer the following question: what factors affect the insurance company's performance in Middle East countries.

Performance refers to the relationship between strategic effectiveness and operational competence of a specific company. Advance production processes; product, services and market management are major purpose of a firm, Batool & Sahi (2019). Financial performance of the firm is very important to attract the concentration of researchers, financial experts and

management of other corporations. It is such a difficult task to select a successful company, that why they have to be concern with the profitability of the firm. According to Doumpou, et al (2012). The financial performance of insurance industry is very important to various stakeholders including agents, policyholders, and policy makers.

Previous Research/Former literature

A study was conducted by Mwangi et al. (2015) to identify the factors that affect the profitability of general insurers in Kenya. The study used multiple linear regressions, with return on assets as the dependent variable, and the study was made for all the general insurance companies in Kenya for the period 2009-2012. Profitability was positively related to influence, equity capital, and management competence index and negatively related to the size and ownership structure. The study did not find a relationship between performance and retention ratio, liquidity, underwriting risk and age. The study recommended that general insurers in Kenya should improve their performance by increasing leverage, equity capital and the quality and competency of their staff.

Zhara et al. (2014) applied structured questionnaires to explore the extent of the application of risk management in insurance companies in Kosovo and its impact on their business performance. Furthermore, the annual reports of the insurance companies are used to evaluate their financial performance.

The hypothesis of this study relates to the impact of risk management in the financial performance of the companies participating in the study. We can say that the information provided may show the situation of the sector and the practices of the insurance market in Kosovo in terms of risk management policies and their influence on modern risk management in the company's financial performance in the insurance market of Kosovo. Hence, these data can be of great interest to any other local companies to prompt them to put risk management at the top of their agenda knowing that insurance companies in this area remain behind developed companies in the region and the EU.

Burca et al. (2014) tried to analyze the determinants of the financial performance in the Romanian insurance market during the period 2008–2012. According to the final results achieved by applying specific panel data techniques, the determinants of the financial performance in the Romanian insurance market were the financial leverage in insurance, company size, growth of gross written premiums, underwriting risk, risk retention ratio and solvency margin.

Merhari et al. (2013) investigated the impact of firm level characteristics (size, leverage, tangibility, Loss ratio (risk), and growth in writing premium, liquidity and age) on the performance of insurance companies in Ethiopia. Return on total assets (ROA) a key indicator of insurance company's performance- was used as dependent variable while the age and the size of the company, growth in writing premium, liquidity, leverage and loss ratio were independent variables. The sample included 9 insurance companies over the period 2005-2010. The audited annual reports (Balance sheet and Profit/Loss account) of insurance companies were obtained from the National Bank of Ethiopia (NBE) and the insurance companies' annual publication reports. The results of regression analysis reveal that insurers' size, tangibility and leverage are statistically significant and positively related with return on total asset; however, loss ratio (risk) was statistically significant and negatively related with ROA. Thus, the insurers' size, loss ratio (risk), tangibility and leverage were important determinants of the performance of insurance

companies in Ethiopia. But, growth in writing premium, insurers' age and liquidity had statistically insignificant relationship with ROA.

Almajali et al. (2012) aimed to investigate the factors that mostly affect financial performance of the Jordanian Insurance Companies. The study population consisted of all insurance companies enlisted at Amman Stock Exchange during the period (2002-2007) which were (25) insurance companies. The data collected was analyzed by using a number of basic statistical techniques such as T-test and Multiple- regression. The results showed that the following variables (Leverage, liquidity, Size, Management competence index) had a positive statistical effect on the financial performance of Jordanian Insurance Companies. The researcher recommended that a high consideration of increasing the company assets will lead to a good financial performance and there was a significant need to have highly qualified employees in the top managerial staff.

Moghadam et al. (2012) compared the performance of different insurance companies in Iran in 9-month period of 2011, because in this competitive environment comparing the performance of the insurance companies and identifying competitive advantages and detecting the best competitors is the most important necessary action to promote the sector of the insurance companies. The findings of this study were as follows: Iran and Asia and Alborz insurance had the most premium manufacturing and insurance companies of Dey & Mihan which had a noticeable growth in the same period of the previous year.

Al shaher et al. (2011) concentrates on evaluating the major factors that affect the commercial banks performance in Middle East region based on factors analysis technique. The authors have chosen 23 variables and analyzed them according to factor analysis techniques (PCA).

The results revealed that the first factor (banks characteristics) is considered the most important factor to banks performance. On the contrary, the sixth factor (religion believes and awareness of banks performance) is considered the least important factor that influences commercial banks performance in Middle East region. The research results suggest that commercial banks in Middle East region should concentrate on the religion beliefs and awareness of banks' performance.

Iswati et al. (2007) used the empirical data from Indonesia Capital Market Directory 2005 that was issued by Jakarta Stock Exchange (JSE). This research used the quantitative analysis approach. The population of the research consisted of the insurance companies at listed in JSE.

The hypothesis test conducted through the regression analysis model with the degree of significance at 0.05. The main conclusion from this particular study was intellectual capital which had influence on the banks' performance.

METHODOLOGY

Generally speaking, the researchers focused on the assessment of the insurance companies' performance by examining their financial ratios and indicators, because these companies are financial institutions aiming to achieve financial returns to maintain acceptable financial level such as; returns on investment (ROI), return on equity (ROE) and other indicators which depend on evaluating the financial performance. However, in this study, the researcher examined the factors affecting the performance of insurance companies by relying on the factor analysis approach, which involved the analysis of individual trends towards the questionnaire statements.

The variables according to this approach can be classified to the rank either ascending or descending order according to their importance from multiple options (Al Shaher, 2011). Also, factor analysis sums up a wide range of variables to a smaller number of unrelated factors with every variable, and explain each factor as a set of variables that are related to a particular property.

Component Analysis Method was adopted as a method of the factor analysis which consisted of the following stages (Norusis, 1993).

Presentation of the answers of the questionnaire in the form of a matrix to represent the respondents, while the columns to represent the study variables.

Correlation matrix between the variables was considered a data matrix.

The association matrix between the variables was analyzed to determine the lowest number of groups of factors that can be changed by the variance between variables. The results were extracted in matrix factors, where the ranks of matrix represented the study variables and columns represented a number of factors that included these variables.

In order to explain the matrix of factors, the first factor was considered the most important because it occupied the largest proportion of the total variation, and it consisted the most important variables of the study, while the second factor followed the first factor in terms of importance, and its variables were in the second rank according to their importance, and so on for the other variables.

The data was collected by designing questionnaire as the study tool, with two parts; the first part was developed to collect the demographic data from the sample members, while the second part included questions on 19 variables which affect the performance of the insurance companies.

Population and Sampling

According to a report provided by Amman Stock Exchange (2019) there are 21 insurance companies listed. As a result of the similarity of the insurance industry in these companies, a random sample was collected for 15 companies and the questionnaire was distributed to 300 employees for the upper and middle levels.

Study Techniques

In this study, the questionnaire was relied upon to analyze the directions of a group of insurance industry specialists. The items in the questionnaire were compatible with the study objectives, as it consisted of 19 questions distributed on the randomly selected sample in order to obtain critical results for the subject of the study.

To measure the estimates of respondents, it was requested to specify the importance of the question from the most important to the least important, that is, the most important question takes weight 19, and the least important of them takes the weight 1

Validity and reliability of the Tool

To measure the strength of reliability between the variables the Cronbach alpha was used. To add, a significant note that values between 0 and 1, and the closer the value to 1, the more it's considered reliable and when it is closer to 0, the more it's considered less reliable Cronbach,

(1951). From the table below the minimum value for the reliability coefficient Cronbach's alpha is 0.611 which is acceptable value to 0.915 which is a high value.

Items	Variables	Cronbach alpha
1	X1 Weakness of the capital of the insurance companies, and the lack of strong financial entities.	0.742
2	X2 Marginal and weak insurance entities, which led to concluding mergers with another banking institution.	0.691
3	X3 Higher premiums reinsurance installments, due to lower retention rates as a result of the weak capital.	0.847
4	X4 Insurance did not play its role as a financing source for investments in the Middle East as the case was in Europe.	0.715
5	X5 Fragility in the relative importance of the insurance industry in the economies of the Arab countries, as the percentage of the insurance premiums is 8% of GDP.	0.881
6	X6 Insurance companies still rely on traditional insurance products, and did not improve their products.	0.799
7	X7 Lack of interest of insurance companies in customers' needs and attitudes, customer satisfaction, and service integration which represent the most important marketing concepts.	0.699
8	X8 Diminutive attention to the development of life and personal insurance, which represents 60% of the volume of insurance premiums in the world.	0.847
9	X9 Lack of interest in raising insurance awareness, besides people's awareness of their insurance rights.	0.811
10	X10 Focusing only on price element and ignoring other issues... etc.	0.915
11	X11 Low per capita premiums that range from \$8.1 in Algeria to \$38 in Saudi Arabia.	0.711
12	X12 Regressive style in work procedures in the insurance sector operations, in terms of applying manual or semi-manual operating approach with an inadequate information system which reduces the size of benefits that have to be maintained from the technological development in the process of rationalizing the administrative decisions and curtailing costs.	0.802
13	X13 Weakness in using the technology in marketing the insurance products.	0.812
14	X14 Lack of appropriate legislations and regulatory system in place in Arab countries in terms of legislation, supervision and control of the insurance industry.	0.692
15	X15 Weakness of administrative performance of high managerial levels in the insurance companies which affects the understanding of the nature of the risks and makes it difficult to expect any possible crisis.	0.611
16	X16 Poor communication level with others, and in human resource management which is essential to achieve the goals by enhancing the staff capacities.	0.669
17	X17 The lack of capable and qualified human resources needed for supervising and regulating the insurance process.	0.728
18	X18 The lack of qualified workers in the productive system in terms of specialized technical fields, which weakens the integration of insurance services.	0.713
19	X19 The existence of a crisis of confidence between the insured and the insurance companies, particularly in certain types of insurance such as auto insurance and to identify the responsibility of the company in determining the amount of compensation.	0.696

Component (Factor)	Initial Eigenvalues			Extraction Sums of Squared Loadings		
	Total	% of Variance	Cumulative	Total	% of Variance	Cumulative %

			%			
1	4.091	21.532	21.532	4.091	21.532	21.532
2	2.454	12.915	34.447	2.454	12.915	34.447
3	2.263	11.912	46.359	2.263	11.912	46.359
4	1.848	9.724	56.082	1.848	9.724	56.082
5	1.687	8.882	64.964	1.687	8.882	64.964
6	1.430	7.525	72.489	1.430	7.525	72.489
7	1.271	6.691	79.181	1.271	6.691	79.181
8	1.012	5.327	84.508	1.012	5.327	84.508
9	0.578	3.040	87.547			
10	0.531	2.793	90.341			
11	0.488	2.567	92.907			
12	0.368	1.936	94.843			
13	0.314	1.651	96.495			
14	0.273	1.439	97.934			
15	0.142	0.750	98.684			
16	0.110	0.578	99.262			
17	0.081	0.428	99.690			
18	0.058	0.305	99.995			
19	0.001	0.005	100.000			

Extraction Method: Principal Component Analysis.

Based on the above table (table 2), after analyzing the whole variables in each factor, we find that these factors explained 84.508% from total variance. The variance was distributed among these following eight factors:

The first factor explained 21.532% from total variance, the second factor explained 12.915%, the third factor explained 11.912%, the fourth factor explained 9.724%, the fifth factor 8.882%, and the sixth factor 6: 7.255%, the seventh 7: 6.691% and finally the last factor explained 5.327%.

Table 3
COMPONENT MATRIX

Variables	Components (Factors)							
	1	2	3	4	5	6	7	8
X1	-0.378	-0.186	-0.269	-0.146	-0.695	-0.315	0.095	-0.008
X2	0.875	0.184	0.169	0.010	0.273	0.027	0.015	-0.019
X3	0.464	-0.497	-0.611	-0.215	-0.220	0.107	-0.027	-0.086
X4	0.449	0.400	0.126	-0.425	0.125	-0.292	0.310	-0.059
X5	0.637	-0.457	-0.116	0.349	0.040	-0.322	-0.269	-0.019
X6	0.437	0.630	0.076	-0.271	-0.246	-0.133	-0.205	0.092
X7	0.427	-0.273	0.523	0.413	-0.254	-0.038	0.262	0.104
X8	0.298	0.559	-0.178	0.316	-0.306	0.368	-0.159	0.042
X9	0.223	-0.249	0.590	-0.209	-0.241	0.415	-0.015	-0.177
X10	0.113	0.364	-0.428	0.502	0.140	-0.001	0.417	-0.131
X11	0.039	-0.341	0.366	-0.549	0.223	-0.043	-0.273	0.343
X12	-0.106	0.220	-0.538	-0.094	0.467	-0.211	-0.167	0.417
X13	-0.138	-0.454	0.055	-0.095	0.497	-0.146	0.535	-0.197
X14	-0.216	0.257	-0.204	-0.449	0.245	0.442	-0.104	-0.508
X15	-0.060	-0.298	-0.053	0.358	0.317	0.620	-0.097	0.291
X16	-0.525	0.408	0.354	-0.077	-0.086	0.160	0.432	0.399
X17	-0.897	-0.007	0.111	0.170	0.005	-0.121	-0.182	-0.102
X18	0.027	0.314	0.547	0.359	0.290	-0.318	-0.341	-0.276

X19	-0.820	-0.013	0.093	0.163	0.004	-0.113	-0.195	-0.105
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Table No.2 above showed that the first factor “Inter develop insurance cultures”, included the most important variables to become the most important factor, these variables were ranked according to their importance as follows: (X₄, X₅, X₁₉, X₂, X₁₇).

The second factor which was “Industry’s dependence on traditional on traditional insurance products” followed the first factor based on its importance which contained two variables (X₈, X₁₆).

While the third factor which was lack of insurance awareness contained the variables (X₇, X₁₂, X₁₈, X₉, X₃).

The fourth factor which was “Low insurance premium” contained the variables (X₁₀, X₁₁).

Referring to the fifth factor to the eighth factor, we find that each of them contained a single variable (X₁, X₁₅, X₁₃, X₁₄) respectively.

RESULTS AND DISCUSSION

Variables	Name of variable	Communalities
X ₁₇	The lack of capable and qualified human resources needed for supervising and regulating the insurance process.	0.897
X ₂	Marginal and weak insurance entities, which led to concluding mergers with another banking institution	0.875
X ₁₉	The existence of a crisis of confidence between the insured and the insurance companies, particularly in certain types of insurance such as auto insurance and to identify the responsibility of the company in determining the amount of compensation.	0.820
X ₅	Fragility in the relative importance of the insurance industry in the economies of the Arab countries, as the percentage of the insurance premiums is 8% of GDP.	0.637
X ₁₆	Poor communication level with others, and in human resource management which is essential to achieve the goals by enhancing the staff capacities.	0.525
X ₄	Insurance did not play its role as a financing source for investments in the Middle East as the case was in Europe.	0.449

The first factor “Inter develop insurance culture “was the most important and contained six variables. The most important variable was the weakness of the presence of cadres capable of supervising and regulating the insurance process. For the variable X₄ insurance did not play its role as a financing source for investments in the Middle East as the case was in Europe, took the lowest importance.

Variables	Name of variable	Communalities
X ₆	Insurance companies still rely on traditional insurance products, and did not improve their products	0.630
X ₈	Diminutive attention to the development of life and personal insurance, which represents 60% of the volume of insurance premiums in the world.	0.559

The second factor was “Industry’s dependence on traditional insurance products” took the second rank in terms of importance. It contained two variables; the most important was the sixth variable which was X₆ (Insurance companies still rely on traditional insurance products, and did not improve their products) followed by the eighth variable which is (Little attention to the development of life and personal insurance, which represent 60% of the volume of insurance premiums in the world).

Variables	Name of variable	Communalities
X ₃	Higher premiums reinsurance installments, due to lower retention rates as a result of the weak capital.	0.611
X ₉	Lack of interest in raising insurance awareness, besides people’s awareness of their insurance rights	0.59
X ₁₈	Weakness of administrative performance of high managerial levels in the insurance companies which affects the understanding of the nature of the risks and makes it difficult to expect any possible crisis.	0.547
X ₁₂	Regressive style in work procedures in the insurance sector operations, in terms of applying manual or semi-manual operating approach with an inadequate information system which reduces the size of benefits that have to be maintained from the technological development in the process of rationalizing the administrative decisions and curtailing costs.	0.538
X ₇	Lack of interest of insurance companies in customers’ needs and attitudes, customer satisfaction, and service integration which represent the most important marketing concepts.	0.523

The third factor according to the importance is “Lack insurance awareness policy” contained five variables, the most important was X₃ (Higher premiums reinsurance installments, due to lower retention rates as a result of weak capital), and the less important factor was X₇ (Lack of interest of insurance companies in the trends and needs of customers, and customer satisfaction, and service process integration which are from the important marketing concepts).

Variables	Name of Variable	Communalities
X ₁₁	Low per capita premiums that range from \$8.1 in Algeria to \$38 in Saudi Arabia.	0.549
X ₁₀	Focusing only on price element and ignoring other issues... etc.	0.502

The fourth factor according to the importance was (Low insurance premiums) contained two variables, the most important was X₁₁ (Low per capita premiums that range from \$8.1 in Algeria to \$38 in Saudi Arabia., while the less important factor was X₁₀ (Focusing only on price element and ignoring other issues... etc. While the factors from six to eight, each of them contained a single variable as follows respectively (X₁, X₁₅, X₁₄).

CONCLUSION

Through analyzing the variables affecting the insurance industry, and in order to assess their performance in the Middle East, the principal component method was used to examine a

large set of variables including four factors, the first factor was (Inter develop insurance culture), which contained the most important variables of the insurance industry according to their priority within the factor, the most important variable in the first factor was X_{17} (The lack of capable and qualified human resources needed for supervising and regulating the insurance process. The latter factor was the fourth factor contained the variable that stands at the fourth degree of importance, thus the less importance variable among the nineteen variables is X_{10} (Focusing only on price element and ignoring other issues... etc.

RECOMMENDATIONS AND IMPLICATION

The study highlighted the variables according to their importance; the researcher recommended to take into account some issues such as the importance of the variables and stressed the need to focus on these variables to improve and upgrade the insurance industry in the Middle East.

Therefore, insurance companies must take into account the shortage in human resources and try to increase and qualify them and organize them to supervise the insurance process. Insurance companies should also use modern methods instead of using traditional methods in the insurance industry and increase the capital in companies and insurance premiums

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