

# A COMPARATIVE STUDY OF THE APPLICATION OF ALTERNATIVE RISK TRANSFER METHODS OF INSURANCE IN SOUTH AFRICA AND ZIMBABWE

*Athenia Bongani Sibindi\**

## Abstract

Alternative risk transfer techniques represent the crown jewels in the risk management arena. This non-traditional method of insurance has gained prominence over the last few decades. Against this backdrop, the present study seeks to unravel the development of the alternative risk financing insurance segment within a developing country setting. The study specifically sets out to compare and contrast the ART insurance market segments of South Africa and Zimbabwe. The study documents that the Zimbabwean market is at a nascent stage of development, whilst the South African market is fully developed. Notwithstanding the prospects for the development of this sector looks bright.

**Keywords:** Alternative Risk Transfer, Non-traditional Insurance, Risks, Derivatives, South Africa, Zimbabwe

*\*Department of Finance, Risk Management and Banking, University of South Africa, P.O. Box 392, UNISA, Pretoria 0003*

*Tel: +27 (0) 12-429-3757*

*Fax: +27 (0) 86-569-8848*

## 1 Introduction

Alternative risk financing represents a spectrum of non-traditional methods of insurance for the management of non-life risks that have gained prominence over the years. Their efficacy is premised on cost effectiveness and innovation. Thus, if insurers recognise that the risk management paradigm is changing from indemnity to value creation and enhancement, they can stem the flow and be lively players in the evolving corporate risk management market place (Doherty, 2000a). The tide is inclining towards the use of Alternative Risk Transfer (ART) techniques. In this article, a comparative study of short-term insurance in Zimbabwe and in South Africa will be conducted to interrogate these issues. The impetus behind the investigation will be to inform on whether Alternative Risk Transfer (ART) techniques are the focal solution to some of the challenges faced by short-term insurance companies. In the final analysis an audit of the techniques shall be conducted to inform of their assets and limitations, with view to proffering suggestions and advice to the would-be benefactors on how to tackle the same challenges.

The economic environment of Zimbabwe has been characterised by downturn, and indeed the global economy has experienced a slowdown during the period 2007 to 2010. As such when insurance companies suddenly embrace Alternative Risk Transfer (ART) techniques, this arouses suspicion and interest alike. It is thus imperative to ascertain the optimal conditions required for this phenomenon to work. This phenomenon which on the face of it, is novelty, must be fully appraised, for the guidance of managers, insurance companies and regulators amongst others.

The factors that are the impetus behind the uptake of alternative risk financing techniques can be enumerated as follows: Firstly, the limitations of traditional insurance have manifested itself in the form of, inadequate underwriting capacity to cater for large risks, narrow scope of cover and failure to provide wholesome cover for financial risks. Secondly, in the aftermath of 9/11 (September 11) attacks insurance rates have stiffened resulting in the cost of insurance shooting through the roof. As a corollary to the foregoing, the economic environment of Zimbabwe has been challenging. Unprecedented levels of inflation were experienced prior to 2008. Yet on the other hand the South African economy has been experiencing steady growth. South Africa witnessed a construction industry boom, in readiness for the 2010 soccer showcase. The question that begs to be answered is: how has short-term insurance coped with such scenarios?

Thirdly the bargaining power of buyers of insurance seems to have a bearing on the development of the ART sector. It is suspected that bigger companies who have sophisticated risks might opt for innovative risk transfer techniques and forego the traditional insurance products. Thus as a rule of thumb, the higher the bargaining power of key buyers, the more inclined will be the insurance company to do as they please. Moreover it must be borne in mind that banks are waiting on the wings to provide service – in strategy parlance, switching costs will be low. In Zimbabwe and South Africa we have seen a trend towards conglomeration, resulting from mergers and acquisitions. This has given rise to a multiplicity of risks and curtailed cover.

The issues enumerated in the above foregoing give the very foundation for this study about ART

techniques. The focal point of the study is to investigate the nature of ART techniques, why insurance companies have or (or have not) used them, or why they should embrace them. In the final analysis it shall become clear whether they are effective and how they should be transacted. The purpose of the present study is to analyse the nature and motivation for the use of ART products in Zimbabwe and similarly for South Africa, to evaluate their practical efficacy and to determine what a comparative study of these two analyses might reveal. The rest of the paper is organised as follows: Section 2 reviews the related literature. Section 3 outlines the research methodology. Section 4 presents the empirical results and Section 5 concludes.

## 2 Review of related literature

Alternative Risk Transfer techniques have evolved over the last fifty years, and it would seem they have endured the test of time, and are not a fashion - that easily fades away, but are a fashionable risk management tool that will carry the insurance industry into the twenty-first century. It becomes imperative that the origins of ART be traced. This probing will unravel the motivation behind the use of ART techniques, the forms they take and the functionality of the ART products.

### 2.1 The origins and evolution of ART

Doherty (2000b) traces the origins of ART techniques to the 1950's. He argues that this was linked to organisations beginning to fully embrace the concepts and process of risk management. Thus there arose the need for corporations to systematise their insurance buying. Managers began to consider systems for loss prevention and later, for the economic control of losses should they occur. There were incentives to do this since insurance prices tended not to reflect the claims experience of the corporation.

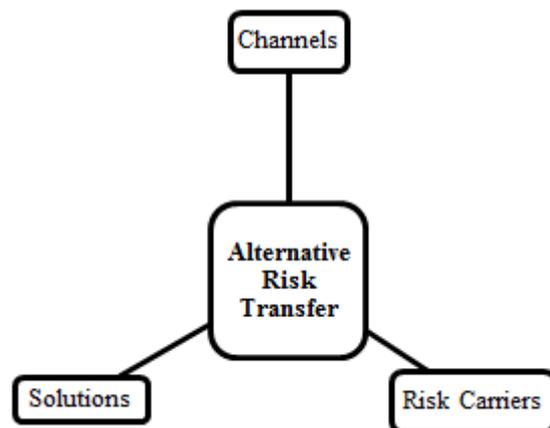
Schanz (1999)<sup>1</sup> contends that the term ART was first coined in the USA. He goes further to say that; initially ART described mechanisms that made it easier for companies to insure their own risks, by means of captives and risk retention groups amongst others. More recently the term has acquired a broader meaning and now encompasses, for example, finite insurance and finite reinsurance as well as risk transfer via the capital markets.

The key features of ART solutions that have evolved over the years can be enumerated as follows<sup>2</sup>:

- Tailored to specific problems.
- Multi-year, multi-line cover.
- Spread of risk over time and within a policyholder's portfolio. This is what makes the assumption of traditionally uninsurable risks possible.
- Risk assumption by non- (re)insurers.

Factoring into account these attributes, the domain of ART techniques is as depicted in Figure 1 below.

**Figure 1.** An overview of Alternative Risk Transfer techniques



Source: adapted from Swiss Re Sigma 2/1999

Firstly, alternative distribution channel to specialised direct insurers and reinsurers are for example companies' own captives, which are potential purchasers of traditional and/or alternative risk transfers products. Secondly alternative solutions embrace finite risk products whose main aim emphasis is on financing rather than the transfer of risks. Multi-year contracts also play an increasingly important role. These solutions combine different classes of insurance such as property and casualty risks. Although these products are not essentially new, they are considered to be alternative as they provide the basis for wider ranging covers. These solutions bundle together insurance, finance and in some cases general business risks as well, in the form of multi-year contracts with aggregate retentions. Other covers that fall into the category of alternative solutions include multi-trigger products, i.e. those which only come into play if insurance and non-insurance loss events occur simultaneously within a specific time frame as well as financing of losses at conditions agreed upon in advance (contingent capital.) Lastly, alternative risk carriers are ultimately capital market investors directly involved in insurance risks. These mainly concern insurance - linked bonds and derivatives.

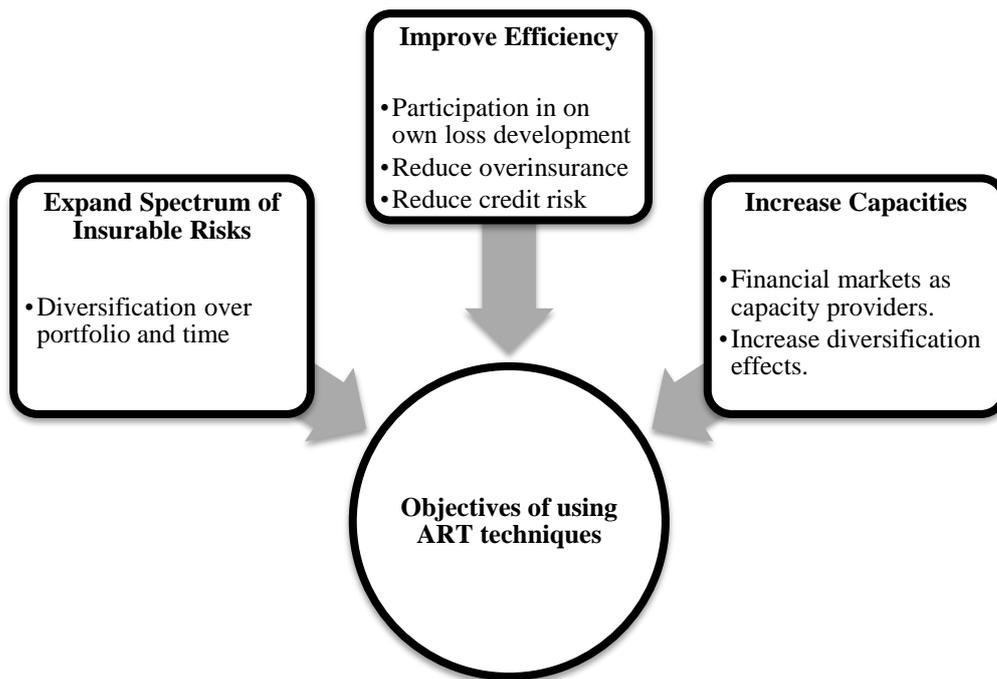
It is instructive to note that ART techniques have evolved to be used by insurance companies, to satisfy the insured and have also evolved to be used by reinsurance companies to satisfy the requirements of insurance companies. As such there are two forms of ART solutions, one peculiar to the cedant and the other peculiar to the insured, in other words, the two classes are - insurance alternative risk transfer and reinsurance alternative risk transfer.<sup>3</sup> Thus the point of convergence for all ART techniques can be enumerated as in Figure 2 below.

<sup>1</sup> Dr Kai-Uwe Schanz was writing in Sigma Number 2/1999 commissioned by Swiss Reinsurance

<sup>2</sup> Schanz *op.cit.*

<sup>3</sup> Punter Alan (1999): The Spectrum of Alternative Risk Financing Opportunities, Aon Group Australia.

**Figure 2.** Reasons for the use of Alternative Risk Transfer



Source: Adapted from Swiss Sigma Number 2/1999

The salient features of Alternative Risk Financing techniques are that the primary objective is that they are developed to complement those already in use in order to improve efficiency of risk transfer. The second goal is to expand the spectrum of insurable risks. The third goal is to generate additional capacity via the capital markets.

Doherty (2000b) propounds that the earliest forms of ART took the form of captives. Increasingly since the 1960's larger corporations have created and used their own in house operation, primarily as a means of co-ordinating insurance buying across the global enterprise. Forent (2004) propounds that the earliest forms of ART programmes developed in response to the hard insurance markets. Companies turned to large deductible, loss sensitive rating and retrospective rating insurance programmes to gain independence. This led to the development of wholly owned offshore captives for large corporations and rent-a-captive for small to medium size companies. He goes on to note that, in the hard insurance, high-interest environment of the early 1990's finite programmes emerged as another finance tool. The motives behind finite programme were similar to captives with additional tax and financial benefits. In the main there are three types of such techniques—finite risk insurance, insurance derivatives and securitisation of insurance risks directly on to the capital markets.

What is instructive to note is that finite programmes began the trend towards a more holistic approach to risk while facilitating the creation of sophisticated coverages that blurred the lines between

financial and insurance markets. According to Culp (2002) finite risk insurances and financial insurances are an extension of conventional insurance in that the contracts typically last for three to five years and they often involve a packaging of different kinds of insurance including some risks that are difficult to place. In addition, finite risk insurance usually poses a profit sharing feature such that if the claims costs of the corporation vary unexpectedly there is some form of *ex post* adjustment in the premium cost. Because of its tailor made character finite risk insurance represented an attempt by insurance companies to develop longer-term risk sharing relationships with corporations. As the name implies, there are limits to the degree of risk transfer in finite risk programs and thus they provide a mezzanine layer of risk financing between self-insurance and conventional types of insurance.

Further, Doherty (2000b) contends that insurance derivatives evolved in the mid 1990's. For a long time, insurance had been seen as a potential area of product development for derivatives, in part because a conventional contract can theoretically be seen as a put option sold by an insurance company. However the development of derivatives as a mechanism of risk financing for corporate risks has been limited for two main reasons. Firstly there are no suitable indices on which derivatives can be based. Secondly derivatives require that the underlying economic variable being tracked is relatively homogeneous. This requirement is often not met for corporate insurance risks since these represent a heterogeneous bundle of risks many of which may be specific to an industry.

In 2000 the only active traded derivative market, was the property catastrophe options market at the Chicago Board of Trade and the Catastrophe Risk Exchange (CATEX) in New York.<sup>4</sup> More recently weather derivatives have been introduced based on indices of rainfall, snowfall and temperature.

One of the latest ART solutions relates to the securitisation of insurance risks directly onto the capital markets. Growth there is likely to continue in the longer term especially for longer-term potential losses facing corporations and for important projects. Two mechanisms for securitisation have evolved, one based on bond instruments and the other on equity instruments. Specialist divisions of insurers and brokers have often collaborated with investment banks to develop tailor made products for corporations to transfer their risks on to the capital markets.

Doherty (2000b) goes on to say that the risk securitisation is likely to expand in the future and companies might switch from bond based to equity based instruments. The theoretical advantage of equity-based instruments is that they are a form of Just-In-Time (JIT) capital, since capital is only raised when a large loss takes place. Equity based products extend the concept of contingent capital that exists in conventional insurance and thus has the effect of removing the capital cost constraint imposed on insurance and reinsurance companies.

The latest form of ART solution to evolve has really captured the imagination of insurance consumers. This is Enterprise Wide Risk Management (EWRM). This is the buzz term across the financial services sector. According to Culp (2002), this represents synthetic contingent capital facilities, which are a collection of contracts together with advisory services supplied to a customer – all of which result in an enterprise wide risk management solution to the firm. Meulbroek (2002) defined EWRM as the process of identifying and assessment of the collective risks that affect a company's value and the implementation of a company-wide strategy to manage them.

What is trite about these definitions is that it is instructive to note that, this requires an organisational endeavour, which requires the participation of everyone. Put in other words, there is an aggregation of effort towards risk management. More to it, companies have three ways of implementing risk management objectives – modifying the company's operations, adjusting its capital structure and employing targeted financial instruments.

Further, Meulbroek (2002) argues that EWRM calls for Integrated Risk Management. As such these terms can be used synonymously. Integration refers both to the combined application of the three tools for implementing a risk management strategy and to the aggregation of all risks faced by the company. Risk management entails managing the company's total

risk, because it is the company's total exposures that determine whether the company can avoid financial distress.

## 2.2 Insurance Alternative Risk Transfer

The development of Alternative Risk Transfer (ART) for corporate buyers has traced the following path:<sup>5</sup>

- Self-insurance
- Captive insurance company, rent-a-captive insurance company and protected cell insurance companies.
- Finite or financial insurance.
- Multi-year, multi-line, aggregate or blended and integrated programs.
- Enterprise wide risk management.

## 3 Research methodology

### 3.1 Research design

The research design used was based on three facets: the research strategy, the research choices and the time horizons. The research strategy was in the form of an analytical survey, while the time dimension was longitudinal (for a 10-year period between 2000 and 2010) and considered just the short term insurance industry. The research choices involved the use of both quantitative and qualitative research methods.

### 3.2 Target population

The target population in this study consist of all players in the value chain of short-term insurance. These are the insurance consumers, brokers, reinsurance companies and insurance companies. However the brokers serve as a proxy for the insurance consumers and as such no attempt were made to make contact with any direct consumer. This study was limited to the Zimbabwean and South African environments.

### 3.3 Sampling techniques

A combination of stratified random sampling and judgemental sampling were used. Stratified random sampling involves the categorisation of the population into strata, which strata exhibit some form of homogeneity (i.e. one or two similar traits.) In this instance the basis of such categorisation was limited to either of the following, market share or the tag of "non-user of ART techniques" or "user of ART techniques". Dividing the population into strata ensured that there was going to be equity in the sample chosen.

For insurance companies in Zimbabwe, the stratification was based on the combination of the user or non-user "tag" and market share. There are

<sup>4</sup> The CBOT was set up in 1992 whilst the CATEX was set up in 1996. The former specialised in options whilst the latter traded in swaps for insurers.

<sup>5</sup> Punter Alan *op. cit.*

currently 25 direct short term insurance companies, 40 brokers and 6 reinsurance companies in Zimbabwe. In South Africa there are 32 captives and over 40 direct short-term insurance companies and 109 broking companies. In addition there is a heavy presence of insurance companies, reinsurance companies that have overseas parent companies. From all the strata two companies were selected for this study.

For Zimbabwe the short term insurance companies that were selected were, Tristar, Nicoz-Diamond, Cell, and Altfin.<sup>6</sup> For the reinsurance segment: Zimre, FM Re, and FBC Reinsurance were selected.<sup>7</sup> In the broking segment: Alexander Forbes, AON Zimbabwe, Trustfin, ZIB, Trust, Eureka and Dolphin were selected.<sup>8</sup>

For South Africa the direct short-term insurance companies that were selected<sup>9</sup> for this study were, Santam, Centriq, Mutual and Federal, Allianz Risk Transfer, Guard Risk, and Outsurance.<sup>10</sup> On the reinsurance front, Munich Re and Swiss Re were selected.<sup>11</sup> On the broking front; Alexander Forbes, Glenrand MIB and AON and ABSA Insurance were selected.

### **3.4 Data collection methods**

This study made use of both primary data and secondary data forms. Each of the forms and the data collection instruments are discussed below.

#### **3.4.1 Primary data collection methods used**

Primary data was collected for the purpose of this research. In the main the primary data was used to help explore the nature of the ART techniques and the motivation behind their use in the two insuring environments. The instruments used to gather primary data were to a large extent the questionnaire and to a less extent interviews.

<sup>6</sup> Nicoz-Diamond is the market leader with 22% of the market. Altfin is in the top 5 and is a subsidiary of a bank holding group- Interfin Holdings. Tristar is a pioneer in the field of ART whereas Cell is a Rent-A-Captive.

<sup>7</sup> In this market Zimre is the leader, FM Re is a pioneer in the field of ART and FBC Re is a subsidiary of a bank holding group.

<sup>8</sup> Alexander, Trustfin and AON Zimbabwe are the major transactors of commercial and corporate risks. The state has a stake in ZIB and hence it transacts major parastatal business. Eureka, Dolphin and Trust transact mostly SME business.

<sup>9</sup> The sampling frame employed was the financial directory [www.fmd.co.za](http://www.fmd.co.za) and the size was determined as per the website [www.sais.co.za](http://www.sais.co.za)

<sup>10</sup> Santam has 7.3% of the ART market. Mutual & Federal is also in the top echelons and has its own subsidiary Centriq that cater for ART products only. Guard Risk is the leader in the ART market accounting for 50%. Alexander Forbes owns Guard Risk. Allianz is a subsidiary of Santam and occupies 3.2% of the ART market. Outsurance is a relatively new player and carries the tag of non-user.

<sup>11</sup> Most of the reinsurance business is channelled through these players in South Africa and they provided a useful source of secondary data on their websites. Hence judgemental sampling was used here.

#### **3.4.1.1 Questionnaire**

The questionnaires were the main instrument of primary data collection used. Three sets of questionnaires were set. These target the players in the value chain of insurance. Since the use of ART techniques is more strategic, the target audience of the questionnaires was middle to senior management. For direct offices as well as reinsurance companies the target audience was Underwriting Managers and Operation Executives whilst for the broking firms it was the Account Executives as well as Operation Executives that were the target. The questions were structured direct and small proportions were open ended. Thus with structured direct questions, the same wording and exactly the same sequence is used for all respondents. The rationale behind using structured questions was to minimise bias and hence focus the research effort. Whilst the use of open ended, i.e. free response type of questions was to minimise the monotony, and hence 'liberate' the respondent to give their unfettered input. This was usually done towards the end of the questionnaires and focused more on the strategic impetus of ART techniques.

#### **3.4.1.2 Interviews**

The interviews employed in this research effort took the form of informal interviews (peer group) and telephonic interviews. Peer group interviews were conducted with contemporaries in the short term insurance industry, to explore the feasibility of such a study. These were more of brainstorming exercises. Telephonic interviews aided triangulation. The respondents, necessitating further probing, might not have addressed some issues in full. Peripheral issues were also interrogated through the use of the telephone. This relates to statistics and matters relating to regulation.

### **3.5 Data analysis and presentation**

The methods used to analyse data were both qualitative and quantitative. Thus quantitative data was converted into qualitative data at times. This helped turn raw data into meaningful information.

#### **3.5.1 Analysis of quantitative data**

Quantitative data in its raw form conveys very little meaning. As such it needs to be processed and presented in a variety of ways. Since this research effort, was mainly a descriptive survey and was a comparative analysis, the most telling processing of the data was graphs, charts and table of statistics. Bar charts, pie charts, line graphs and histograms were indispensable in establishing the trends and in comparison.

#### **3.5.2 Analysis of qualitative data**

This included all non-numeric data or data that has not been quantified. This particularly related to fitting secondary data into this research effort as well as the

responses from open-ended questions. Triangulation of data analysis methods was employed in this study.

#### 4 Empirical results

In this article we make use of descriptive statistics to compare and contrast the trends in the development of the alternative risk transfer insurance segments in South Africa and Zimbabwe.

#### 4.1 Analysis of respondents

The number of questionnaires returned was general satisfactorily. Maybe this was as a result of the mode of transmission that was used (email was used) in most cases. Table 1 shows the distribution of the questionnaires and the success rate.

**Table 1.** An analysis of respondents

Type of Company	Zimbabwe			South Africa		
	Questionnaires sent	Questionnaires returned	Success Rate%	Questionnaires sent	Questionnaires returned	Success Rate %
Direct Insurance	4	3	75	6	4	67
Broking	7	5	71	3	2	67
Reinsurance	3	2	67	2	2	100

Source: Author's construction from survey results

#### 4.2 The type of ART products being used

This research effort sought to investigate the types of products being offered by insurance and reinsurance companies in Zimbabwe and South Africa and hence inform whether they are different or not. This would then have served as a springboard to tackle the motivation behind their use. Further the interrogation of the make-up of ART techniques being used in these markets would have helped identify the stage of development of the ART segment in those markets. Questions were set for all the players in the value chain to help address this question. The results of the survey are shown in Table 2.

In Zimbabwe there is just one cell-company whilst in South Africa there are 32 captives and 7 cell insurance companies. Alternative risk transfer seemed

to be limited to multi-year products and only two direct companies transacting finite insurance and two reinsurers transacting finite reinsurance (Refer to Figure 3). Only one direct company was offering EWRM in Zimbabwe. In South Africa, finite risk products were popular with 75% of direct insurance companies indicating that they offer them. All the brokers in South Africa also indicated that they use ART techniques to manage the risks of their clientele. All the reinsurance companies also indicated that they offer finite reinsurance to their clients. However these results have been treated with caution in that particularly a small sample in relation to the size of the South African market was developed for economy of research.

**Table 2.** A checklist of the ART products being used in Zimbabwe and South Africa

ART Product	Zimbabwe	South Africa
Captives	Yes limited to insurance pools, and cell captives	Yes all classes of captives.
Finite (Re)Insurance	Yes limited to insurance managed funds (self-funds)	Yes all classes.
Enterprise Wide Risk Management	Very limited	Yes
Insurance derivatives.	Yes very narrow in scope	Yes
Contingent Capital.	No.	No.
Insurance Linked Securitisation	No.	No
MMPs	Yes limited to multi-year covers	Yes both multi-year and multi-line covers.
MTPs	No	Yes

Source: Author's construction from survey results

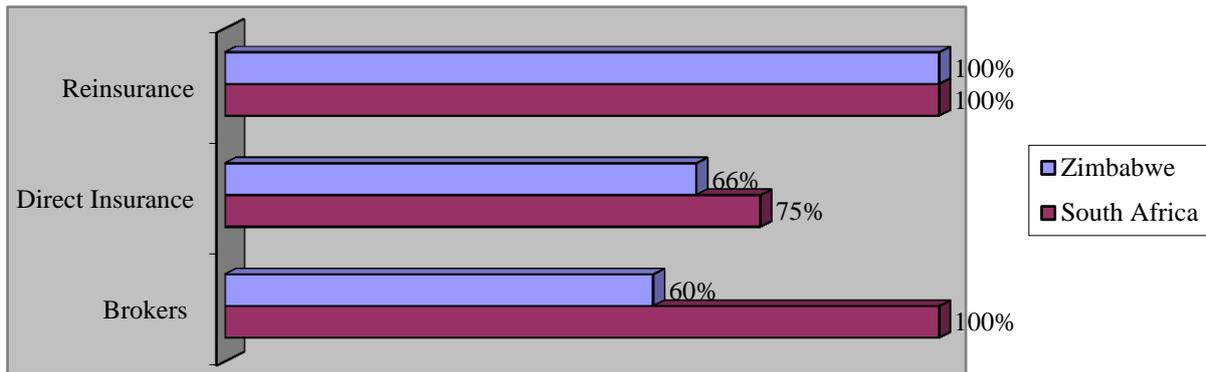
#### 4.3 The motivation behind the use of ART techniques

The motivation for using ART technique varies from organisation to organisation and from one environment to the other. The imperatives of different environments are never a carbon copy. To unravel the impetus behind the use of ART was never a straight-

line affair and required triangulation<sup>12</sup>. The starting point was to determine whether the organisation was a user or non-user of ART techniques. Figure 3 represents this information.

<sup>12</sup> Questions were set for the reinsurers, direct insurance companies as well as the brokers, to probe the motivation behind their use.

**Figure 3.** The proportion of users of ART solutions

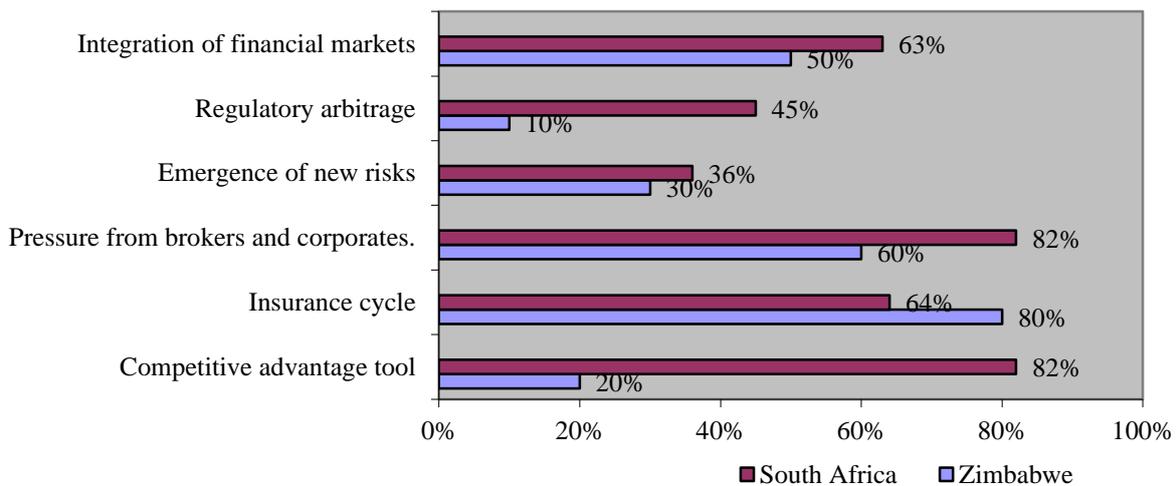


Source: Author's construction from survey results

It was unearthed that the South-African market has embraced the ART solutions more than its Zimbabwean counterparts. On the direct insurance side 75% indicated that they were using ART solutions as compared to 66% in Zimbabwe. Further all the brokers in South Africa revealed that they had used ART solutions at one time as compared to 60%

of the brokers in Zimbabwe. On the reinsurance side all the players indicated that they had encountered ART solutions and challenges. When they were further probed it was determined the median times that the organisations began offering ART solutions in Zimbabwe was between 5-10 years ago, whilst for South Africa it was between 15 –20 years ago.

**Figure 4.** The key drivers of ART



Source: Author's construction from survey results

From an analysis of the respondents view, it was unearthed that the key drivers of the ART segment are not that dissimilar in the two environments. The pressure from corporates and brokers (82%), insurance cycle (80%), integration of financial markets (63%), and the quest for a competitive advantage tool (82%) were the strongest forces in the South African market. In Zimbabwe, this concept has mainly been embraced chiefly to deal with the insurance cycle (80%). Cost dynamics have been pushing the insuring consumers towards the ART segment. Brokers have also been at the forefront of the development of the ART sector in Zimbabwe. Unlike with South Africa where there are many big corporations, Zimbabwe has a few of big corporations, mainly in the mining segment; hence maybe the demand side response is relatively weak.

#### 4.4 The efficacy of ART solutions

Having addressed the motivation behind using ART solutions, their effectiveness was tested. The responses of the respondents were varied and included the following benefits derived from ART solutions.

- ART solutions are flexible and tailored to suit the needs of client.
- They reward good housekeeping of risk, hence are experience based
- Increased insurance capacity.
- Manage new risks or are used as a front for the new risk classes until sufficient data has been gathered to write them using traditional insurance.

- They complement traditional insurance products and hence cross subsidise them in the event of a swing in the insurance cycle.
- Arbitrage exist between the traditional segment and the ART segment
- They can be used as a competitive advantage tool to outwit competition.

- They can be used to gain a foothold in capital markets.
- ART business is profitable.
- The loss ratios are low.

The top 5 strategic reasons for embracing ART techniques are shown in the Table 3 below. These are in ranked order, with 1 representing the most important.

**Table 3.** The top 5 strategic reasons of embracing ART techniques

<i>Strategic Goal</i>	<i>Zimbabwe</i>	<i>South Africa</i>
To gain competitive advantage. (Defend market segment)	4	1
To achieve cost efficiency (Cost leader strategy)	1	3
To gain market share.	2	1
To counter the competition from banks and finance institutions.	3	4
To increase shareholder value.	5	5

Source: Author’s construction from survey results

However the challenges that were proffered include the following:

- Some ART products are expensive and hence generally inaccessible to the insuring corporates.
- Some ART products are not tailor-made and hence do not really address the risk financing requirements of corporations.
- Companies have not gathered enough information to optimally price some ART products.

#### **4.5 The influence of the macro and micro-environments in the use of ART solutions**

The macro and micro-economic environments have promoted the use of Alternative Risk Transfer techniques albeit in different ways. In Zimbabwe there has been a knee-jerk approach to the development of ART solutions. 80% of the respondents highlighted that the inflationary environment prevalent between 2000 and 2008 rendered the environment generally uninsurable. Insurance companies suffered from ‘adverse selection’ by the environment if the reinstatement value condition is triggered. The premiums collected became disproportionate to the risk carried. As one respondent put it, insurance values continued to be eroded and hence the self-managed funds became popular. This was exacerbated by the state of the market. The Zimbabwean market is currently experiencing a soft market and hence there is rampant rate cutting. This has resulted in increased M&A activity. This gravitated the market towards an oligopoly structure, with 70% of the business transacted by the top 5 companies.<sup>13</sup>

In South Africa the market is hard and it is expected that the cost of insurance will rise. On the macro environment, inflation is generally low

hovering around 3 to 5% target band. Insurance companies have turned to the ART segment to gain competitive advantage. (82%) of the respondents highlighted that they were embracing ART to achieve competitiveness in their spheres of influence across the value chain. There has been further activity in the M&A arena with the top companies acquiring specialist risk transfer companies to unlock shareholder value.

High solvency margin requirements have curtailed the capacity of insurance companies in both environments. Although it was not commonly chosen, from triangulation it was revealed that the capacity to write risk was generally inadequate especially in the Zimbabwean environment. However companies do not seem to have conceived securitisation as a solution to this challenge. This was evidence by those respondents who highlighted that they were experiencing solvency problems but who did not go on to proffer securitisation as a solution. Further in both environments it would seem that the bargaining power of intermediaries is very high. Thus brokers have shaped the direction of the ART market. This has promoted the development of ART solutions.

#### **5 Conclusion**

The present study has demonstrated that insurance companies should embrace ART techniques as they the crown jewels in the risk management arena. Further, they must be best understood as compliments rather than substitutes to traditional insurance products. The research findings also document that, on the one hand the Zimbabwean ART market is at its nascent stage of development whilst on the other hand the ART segment is fully developed in South Africa. We also wish to proffer policy advice as follows—the functionality and effectiveness of ART solutions is anchored on healthy, highly liquid financial markets. As such, it is imperative that the authorities on the monetary side and those superintending over the

<sup>13</sup> The most visible mergers were that of Nicoz and Diamond Insurance Companies, Orion and Strategis as well as Zimnat and Lion followed by that of RM and CGU. The market leader is Nicoz-Diamond which accounts for 22% of the short-term insurance market.

capital markets endeavour to develop such markets. For example a central depository has been mulled for the Zimbabwe Stock Exchange since time immemorial. Until such interventions, the development of the ART segment in the Zimbabwean market shall be stalled. Thus if the restrictions of capital flows are unencumbered between South Africa and Zimbabwe, that is bound to stimulate the ART sector.

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