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Globalization and insurance activity: Evidence on the industrial and emerging countries



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ABSTRACT

This study applies panel cointegration with cross-country dependence and causality tests to uncover the extent and the magnitude of the relationship between insurance penetration and globalization. The results first confirm evidence of the long-run relationship between insurance market activities and globalization. Second, we find positive impacts of all three globalization indices on life and non-life insurance penetrations, and globalization has a larger impact on insurance market activities in the industrial countries than in the emerging countries. Finally, the results of panel causality tests roughly show bidirectional causality between insurance market activities and globalization in the long run.

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1. Introduction

In recent decades, an increasing concern and interest has been seen on the economic and financial impacts of globalization, which have strengthened positive international correlations (Gabbi, 2005) and enhances international migration providing banks for a new opportunity of growth (Gleisner, Hackethal, & Rauch, 2010).¹ Due to the impacts of business globalization of economic areas and the

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¹ Globalization can be simply defined as a gradually developing interaction and integration of economies, finances and societies around the world (Das, 2006) and as an increased openness of national economies to trade, foreign investment and financial flows (Arndt, Crowley, & Mayes, 2009). It can make commodity and finance markets more competitive, which speeds up the transmission of productivity growth across national borders, and it may also stabilize output by making producers able to service a diversified global market (Mishkin, 2009).

growing interdependence among people worldwide on the insurance markets that allow for creating a global insurer, the globalized world economy can foster the globalization of insurance services (Anđelić, Čosić, & Đaković, 2010) and a well financial environment can give opportunities for the development of the insurance industry. Furthermore, the world's financial markets have been increasingly integrated due to globalization, and it weakens the protection of investors' portfolios against local and/or national crises (Silvennoinen & Teräsvirta, 2009). Alexander (2005) and Broome and Markhan (2000) note that new risks have been obtained as the deregulation of financial operations. These global risks could also lead to insurance globalization. To confront international risk diversification, insurance companies will make their insurance products more diversified. Thus, globalization will be an inevitable factor in the process of the insurance market development.

Since the development of the insurance market and globalization play an increasingly substantial role in the economic and financial sectors,² “Do the different aspects of globalizations (i.e. economy, society and politics) have different effects on the life and non-life insurance market developments?” and “Are these effects influenced by countries with different income levels?” are both worthy of investigation. By answering these questions we hope to improve understanding of the insurance-globalization nexus.

To the best of our knowledge, the existing studies document the possible impacts of globalization on insurance market development from theoretical viewpoints (Enz, 2000; Litan, 2001; Pearson, 1997; Schiro, 2006). Schiro (2006) indicates that efforts tend toward more open and transparent consultation in all aspects, and it behooves the leaders of the insurance industries to promote dynamic regulation responding to market forces and foster innovation. Pearson (1997) argues that a decrease in the cost of communication and storing and evaluating information have deeply influenced the insurance sectors. Litan (2001) also shows that low-cost communication and deregulation in the financial markets has enlarged the financial scope internationally. In addition, the Internet's prevalence provides consumers in the world with more information and diversified choice for insurance products, which make the possibility of homogeneous insurance products in international insurance markets more likely.

Life and non-life insurance (also known as general insurance) activities may affect economic activities through different ways because they are closely related to, respectively, economic individuals and corporations who suffer from different kinds of risk. On the other hand, life insurance companies facilitate long-term investments while non-life insurance companies invest in the short-term financial assets. Life insurance is a form of insurance coverage that pays out premiums to the insured or their specified beneficiaries upon a certain incident. In contrast, non-life insurance consists of insurance policies that protect the insured against losses and damages other than those covered by life insurance such as property-liability, motor vehicle, marine, pecuniary loss, and aviation. To date, except for Lee and Chang (2012), Chang, Cheng, Pan, and Wu (2013), and Chen, Cheng, Pan, and Wu (2013) in the empirical evidence, no published study has investigated the impacts of globalization (overall and sub-dimensions) on the insurance market. Thus, this study tends to empirically investigate the relationship between insurance market activities and globalization, taking into account the effects that life and non-life insurance might have, due to the distinct benefits they provide to households and corporations.

The paper is distinct from existing papers in the sense that it compares the relationship between the insurance market and globalization with country groups rather than for individual countries. We decompose world data of this effect into two different groups of countries according to the level of income development. Compared to Lee and Chang (2012) who only study life insurance markets, and Chang et al. (2013), and Chen et al. (2013) who only adopt overall globalization index, we also examine the long-run and dynamic relationships between non-life insurance market and three sub-indices of globalization. In this study, we classify our sample into industrial and emerging countries to find out whether there are different impacts of globalization indices on the developments of insurance markets for countries with different income levels. In addition, we employ the Granger causality tests and

² Since 1950, the global insurance industry has seen an annual growth rate of over 10%. In addition, in the life and non-life insurance markets, global players, i.e. Allianz and AXA have emerged, and reinsurance companies, i.e. Swiss Re and Munich Re, have traditionally served global markets (Schmid and Walter, 2012).

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