THE INFLUENCE OF FOREIGN INVESTMENTS ON THE ACTIVITY OF INSURANCE COMPANIES AS INSTITUTIONAL INVESTORS IN THE CAPITAL MARKET OF THE REPUBLIC OF MOLDOVA

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Abstract: *In this article were investigated the peculiarities* of *insurance industry internationalization, were examined the main factors which influence on attracting of foreign investments by the insurance companies and were revealed the advantages and disadvantages of foreign investments in insurance sector. To analyze the perspectives of stimulation of insurance companies' activity as institutional investors in the capital market of the Republic of Moldova, in article was investigated international experience of investment activity of different insurance sub-industries including life and health, property and casualty, multiline, reinsurers and insurance brokers, was analyzed investment practice of insurance companies in the Republic of Moldova and was revealed the impact of foreign investments on their investment portfolio. In order to apply the best international experience in the national financial market, in this study, based on such research methods and instruments as: logical analysis of theoretical and practical materials, documentary method, analogy and grouping, quantitative and qualitative data method, method of synthesis, comparative analysis, were revealed the features of domestic insurance companies' investment activity and offered recommendations on its stimulation, taking into account the best international practice.*

Key words: *capital market, foreign investments, insurance companies, institutional investors*

JEL Classification: F21**,** G22, G23, O16

1. INTRODUCTION

Insurance companies, as institutional investors, are very important participants in the financial market, inclusive the capital market. They have a very important role as they contribute to the strengthening of competition in the financial market, stimulate financial innovation, strengthen corporate governance, contribute to increase market integrity, pressure for modernizing market infrastructure, encourage the development of regulations.

Due to increased risk of devastating natural disasters and terrorism, which is now the dominant influence on the insurance sector, in the global market there is integration of insurance companies. This leads to the formation of market giants who have huge resources expressed in billions of euros. Thus, they become key players in the global capital markets and have a huge impact on price movements within these markets. Insurance was one of the first industries that became international [Balaban M., 2015]. Deregulation, privatization and liberalization have facilitated globalization of risks and insurance services [Njegomir & Stojić, 2012]. The global insurance industry is facing increasing competition, which has put significant pressure on companies to become more efficient, enhance their technology-related processes and alter their business models. Globally, most insurance companies are trying to enhance the efficiency of their underwriting process, cut their overheads and reduce claims leakage since returns from investment are shrinking. With high competition in the insurance industry, companies strengthen their product lines, investment strategies and corporate infrastructure [Hasan A., 2015].

2. Research theoretical aspects

The insurance companies from developed and developing countries actively participate in international financial integration. The foreign investments are especially important for developing countries where the internal sources of investment are not enough to meet the growing demands of domestic financial market modernization. To attract foreign investments governments from these countries elaborate and implement a wide range of measures, taking into consideration that exist

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many factors which influence on attracting of foreign investors. Besides cultural differences between foreign and domestic institutions, transaction costs, market transparency, general macroeconomic stability, the main factors impact on institutional investors decision regarding their international activity in foreign markets comprise:

a) Political: political stability or uncertainty; attitude of the host government towards foreign private investment, national standards of treatment of foreign affiliates; special inducement for foreign investors, such as tax holidays grants, loans at favourable rates, tariff protection etc.

b) Legal: the rules and regulations pertaining to the entry and operations of foreign investors; restrictions, on bringing home ("repatriating") earning or profits in the form of dividends, royalties, interest or other payments; regulation of the stock and bond markets; investors protection regulation.

c) *Exchange control:* convertibility of local currency; exchange rate stability.

d) Taxation: existence of a double-taxation agreement between the host country and institutional investor country; existence of discrimination taxation of foreign investors; withholding tax payable on remittances; taxes on capital gains etc.

e) Finance: national economic growth rates; the functioning and efficiency of local markets; depth and sophistication of the capital market, its liquidity; local sources of capital and interest rates payable; rate of inflation; the quality of domestic accounting, as well as accounting requirements and conventions [Biloocaia S., 2018].

Even the *foreign investments* impact on the financial market of emerging economies still remains one of the disputable themes of researchers, for the insurance sector, they have the strong positive effect, providing the following *advantages:* promotion of integration processes in the world financial market; expansion of the financial resource base; introduction of modern technologies to the insurance sector; transition to global standards of financial culture; improvement of the quality of services and expansion of the range of financial services; increase in the capitalization of the insurance sector, resulted in formation the system of large domestic institutional investors; better transparency of ownership and accounting; increase in competition in insurance services; more expertise and professionalism in domestic insurance sector; facilitation of the transition to the international standards of supervision and regulation; reduction in risk and effective financial support during the crisis by the parent companies; increased insurance penetration; greater mobilization by insurance companies of the national saving and their channelization into investments in different sectors of the domestic economy etc.

The main *disadvantage of foreign investments* in domestic insurance sector comprise: strengthening of the negative impact of financial globalization; threat to economic independence, increased uncertainty and financial market dependence on foreign capital; increased impact of external shocks and financial crises of other countries on the domestic economy, uncontrolled outflow of foreign capital; realization of the interests of other countries, ignoring the priorities of domestic country; reduction of competitiveness of domestic insurance companies [Lyutiy & Borovikova, 2013].

3. Proposed research methods

Presented in this article investigation was implemented based on such research methods as: *general-scientific methods of cognition, logical analysis of theoretical and practical materials,* documentary method, analogy and grouping of quantitative and qualitative data method, method of synthesis and comparative analysis method. Analysis is grounded on the data obtained from Organisation for Economic Cooperation and Development (OECD), World Bank, National Commission for Financial Markets (NCFM) etc.

4. Research of empirical aspects

Insurance companies are long-term investors whose investment process consists of strategic asset allocation decisions, which determine broad portfolio distributions across asset classes, such as bonds and equities as well as tactical asset allocation that involves deviations from the basic asset categories to exploit short-term profit opportunities. Taking into consideration above mentioned role of insurance companies in developed economies, as one of the largest institutional investors in the financial market, significantly contributed in savings mobilization and their canalization in long term investment in social and infrastructure sectors, thus stimulating economic growth, in this article is analysed experience of insurance companies' investment activities on example of United States financial market, where insurance companies are one of the most influenced investors. Was analyzed five sub-industries: life and health (LH), property and casualty (PC), multiline (ML), reinsurers (Re) and insurance brokers (IB). The tables reported below provide the time-series averages of the corresponding annual common-size analyses [CEASA, 2016]. Table 1. provides a common-size presentation of the primary asset groups. The largest asset class is investments. This is true for each of the sub-industries, except insurance brokers.

***Table 1.* Primary asset categories of insurance companies**

	All	LH	PC	ML	Re	IB
Cash	2%	2%	3%	1%	4%	2%
Investment Assets	56%	57%	62%	44%	70%	26%
Accounts Receivable (including premium)	3%	1%	6%	2%	5%	37%
Reinsurance Assets	5%	2%	9%	7%	11%	0%
Intangible Assets	2%	1%	4%	1%	0%	20%
Deferred Policy Acquisition Costs	4%	4%	2%	4%	4%	3%
Separate Account Assets	20%	28%	2%	35%	0%	0%
Other Assets	8%	5%	12%	6%	6%	12%
Total Assets	100%	100%	100%	100%	100%	100%

Source: elaborated by the authors based on [3]

This format reveals asset composition differences across the sub-industries. In particular, for LH insurers, investment assets constitute almost 60% of adjusted assets, and deferred policy acquisition costs constitute 4%. In contrast, for PC insurers, investments account for 62% of adjusted assets, and DAC constitute 2%. Instead, PC insurers have substantial reinsurance assets, receivables, and other assets (Table 2).

***Table 2.* Investment assets of insurance companies**

	All	LH	PC	ML	Re	IB
Short term investments	0%	0%	0%	0%	1%	0%
Investments in securities	83%	80%	89%	85%	82%	38%
Investments in loans	9%	15%	2%	5%	3%	0%
Investments in real estate	1%	1%	0%	0%	0%	0%
Other investments	7%	4%	9%	10%	14%	62%
Total Assets	100%	100%	100%	100%	100%	100%

Source: elaborated by the authors based on [3]

Most insurers do not report a separate category of short-term investments but instead include them in "cash" or "investment in securities." *Short-term investments* include primarily short-term fixed income instruments such as commercial paper and T-bills. These investments are reported at either fair value or amortized historical cost which, due to the short-term nature of the instruments, approximates fair value. Interest income is calculated using the effective interest rate method. *Investments in Securities* include all investments in fixed income securities, passive investments in equity securities (i.e., other than control or significant influence investments), and investments in other securities (Table 3.).

***Table 3*. The structure of securities in investment portfolio of insurance companies**

	All	LH	PC	ML	Re	IB
Fixed income securities	91%	97%	86%	90%	94%	86%
Equity securities	7%	2%	13%	10%	6%	14%
Other securities	2%	1%	1%	0%	0%	0%

Total investments in securities	100%	100%	100%	100%	100%	100%

Source: elaborated by the authors based on [3]

Investments in debt securities constitute the majority of securities holdings and, for many insurers, the majority of reported assets. Investments in equity securities are a distant second. PC insurers have significant investments in equity securities, which are generally very liquid. LH insurers invest almost exclusively in fixed income instruments.

Fixed income securities (debt securities) comprise: cash equivalents - liquid low risk investments with maturity of three months or less at the date of purchase; held to maturity - intent and ability to hold the securities until they mature; trading - bought and held for the purpose of selling them in the near term in order to profit from short-term price movements; available for sale - all other. *Equity securities* include: trading - bought and held for the purpose of selling them in the near term in order to profit from short-term price movements; available for sale - all other. *Investments in loans and leases* include mortgage loans, policy loans, and other loans. Mortgage loans constitute the majority of loans, but policy loans are also quite significant [CEASA, 2016].

Insurance sector are underdeveloped in emerging markets (Table 4). But the importance of institutional investors (both foreign and domestic ones) in emerging financial markets is increasing, the number of this type of investors, the volume of assets under their management, their profitability is steadily growing. The main factors driving institutional investors growth in emerging markets comprise: a growing urban middle class; per capita income growth; rapid technological developments, innovative services based on smartphones and tablets utilization; the emergence of new micro-insurance, pensions etc. products; regulatory changes moving to strengthen solvency, protect consumers, foster the development of new products etc.

***Table 4*. Financial assets of insurance corporations, as a percentage of GDP, %**

	007	008	009	010	011	012	013	014	015	016	017
Belgium	4.0	0.9	7.7	8.1	7.4	3.3	2.5	9.1	7.4	4.0	1.0
Czech Republic		0.2	1.5	1.6	1.5	1.3	1.7	2.4	1.8	1.1	0.5
Estonia	.0	.1	.7	.8	.6	.6	.2	.7	.3	.9	.0
France	5.3	9.2	0.8	4.8	1.0	9.5	03.1	12.5	12.6	20.6	20.8
Germany	7.4	4.3	7.5	7.8	6.5	9.5	1.1	4.0	2.7	3.4	1.8
Hungary	.8	.9	.9	.9	.3	.5	.2	.3	.9	.9	.6
Japan	5.0	3.4	0.0	9.3	1.1	4.9	9.1	2.7	7.8	9.8	9.1
Lithuania			.7	.1	.9	.2	.7	.7	.9	.4	.5
Netherlands	3.0	2.6	3.8	5.0	5.3	0.2	6.7	2.9	9.5	6.7	1.5
Poland		1.0	0.4	0.3	.5	0.3	0.3	0.6	0.4	.9	
Slovenia			3.9	4.9	4.9	7.2	8.0	8.9	8.0	8.3	7.9
Switzerland	2.5	3.1	0.7	0.7	3.1	7.5	4.3	9.0	5.8		
United States	3.8	9.5	3.0	3.6	3.3	3.7	5.1	5.0	5.8	6.6	7.5

Source: elaborated by the authors based on [8]

Foreign institutional investors play an important role in the improvement of the institutional infrastructure of emerging market economies and have an important impact on the development of securities markets, notably stock markets. Despite the existing risks when investing in financial markets of developing countries, such as: volatility, illiquidity, currency devaluations, unanticipated political and economic developments, still low or middle per capita income, an economy that has not yet been industrialized, underdeveloped financial infrastructure, there is a dramatic increase of portfolio flows from institutional investors into emerging markets, with professionally managed investment funds taking the lead. This undoubtedly contribute to the fact that domestic institutional investors are starting to play an increasingly important role. However, their role is as yet fairly modest and, therefore, there is considerable scope for an expansion of both the domestic institutional sector and the domestic securities market.

Insurance is a significant sector of the non-banking financial market in the Republic of Moldova. The national *insurance market* has undergone an important milestone by endorsing and putting into implementation of some amendments to the normative framework aimed perfectation of financial services provided by insurance companies, quality of intermediation, mechanism and financial remediation, recovery instruments as well as increase insurance sector solidity. At the same time, on the insurance market of the Republic of Moldova, which is still underdeveloped, mandatory insurance of motor third party liability is still dominant (CASCO, "Green Card"). Thus, in 2016, from a total insurance portfolio of about 1.35 billion lei, cumulative amount of paid insurance claims for the motor insurance (motor third party liability insurance and insurance of road vehicles (CASCO) amounted to 442.6 mln lei or 88.4% of the total compensations paid in non-life direct insurance in value of 500.7 million lei, for "Green Card" were paid 310 mln lei of gross premiums.

The factors influenced on these tendencies include: immaturity of the domestic insurance market, socio-economic and humanitarian reasons, low living standards and lack of an insurance culture. For example, the dominant part of housing insurance contracts' is represented by foreign citizens, international firms and organizations, as well as holders of mortgage credit agreements for whom the house insurance is mandatory. The main indicators of insurance market evolution during 2012-2017 in the Republic of Moldova are demonstrated on table 5.

***Table 5*. The main indicators of insurance sector' evolution in the Republic of Moldova, 2012-2017**

	2012	**2013**	**2014**	**2015**	**2016**	**2017**
Number of insurance companies	18	16	15	15	16	16
Number of insurance/ reinsurance brokers	76	75	70	75	70	60
Social capital of insurance companies, mln. lei	556,7	469,3	505,5	525,7	562,7	594,18
Foreign investments in the social capital of insurance companies, mln. lei	143,5	106,1	133,8	202,9	210,4	108,6
Weight of foreign investments in attracted capital, %	25,6	22,6	26,5	38,6	37,4	18,2
Investments in securities, %	16,9	26,1	32,8	33,2	33,5	46.2
Net assets of insurance companies, mln. lei	1241,8	1068,9	1130,5	1154,3	1304,4	1373,8
Volume of gross written premiums, mln. lei	1089,3	1198,9	1203,6	1228,5	1380,1	1441,9
The degree of insurance penetration, %	1,2	1,2	1,1	1,01	1,03	0,96
The insurance density (lei/nat. person)	306,0	337,0	338,3	345,7	388,7	406,1
Compensations and insurance indemnities paid, mln. lei	430,5	432,4	513,6	386,6	519,1	506,1

Source: elaborated by the authors based on [7]

According to the informations presented in NCFM Annual Reports, during 2012-2016 all main indicators, besides degree of insurance penetration, demonstrated growth, stimulating foreign investors for actively investments in insurance companies in the Republic of Moldova. In national insurance sector, in 2017, the volume of gross written premiums increased to 1441.9 mln. lei, the insurance density grew to 406,07 lei/nat. person. Investigation revealed, that the companies with significant share of foreign capital, in securities market, make investments mainly (some of them – only) in Government securities. The share of foreign investments in attracted capital by the domestic insurance companies, significantly decreased, from 37,4% in 2016 till 18,18% in 2017 due to implementation of National Commission for Financial Markets' resolutions, courts decisions etc. regarding the shares of shareholders of Alliance Insurance Group and Moldasig resulted from the revealed noncompliance with national legislation.

Also, the results of investigation demonstrates, that growth of investment activity of the domestic insurance companies in the capital market of the Republic of Moldova, correlated with increase of share of foreign investments in insurance companies' social capital during 2012-2016, continued in 2017, in condition of foreign investments decreasing (see Table 6).

The dynamic of the evolution of structure of insurance companies assets demonstrates that the share of assets saved by domestic companies in securities within 2012-2017, increased from

17% to 46% and its absolute values remained unchanged, despite the decreased of total invested assets from 2265 mln.lei in 2016 to 1706 mln.lei in 2017, the share of allocated capital into bank deposits decreased from 35% to 18%. The volume of capital invested by the insurance companies as institutional investors on the capital market grew from 152.9 mln.lei in 2012 to 788.2 mln.lei in 2017, the volume of capital invested in bank deposits, decreased from 317.5 mln.lei to 310.0 mln.lei in the same period [NCFM, 2018].

***Table 6.* The evolution of the structure of assets admitted to represent the insurance reserves and the minimum solvency margin for 2012-2017**

Indicators	**2012**		**2013**		**2014**		**2015**		**2016**		**2017**	
	mln. lei	**%**	**mln. lei**	**%**	**mln. lei**	**%**	**mln. lei**	**%**	**mln. lei**	**%**	**mln. lei**	**%**
Securities	52,9	6,9	84,3	6,1	98,4	2,9	05,7	3,2	58,5	3,5	788,2	46,2
Bank deposits	17,5	5,1	23,0	0	08,8	5,5	98,1	8	94,2	6	10,0	18,2
Available in bank accounts and in cash	0,9		9,3		7,5	,6	58,7		40,4		3,4	5,5
Land and buildings	85,6	1	99,9	7,9	26,9	8,7	55,2	7	00,7	8	25,1	13,2
Receivables related to subscribed premiums	4,0		3,8		8,4	,6	25,9		57,4		2,7	5,4
Reinsurer's share	30,4	4	27,3	2	42	1,7	79,8		13,7	,5	96,6	11,5
Total	01,3	00	087,6	00	212,0	00	123,4	00	265,0	00	706,1	100

Source: elaborated by the authors based on [7]

5. CONCLUSION

According to the results of implemented analysis, in the Republic of Moldova, foreign investors provide for domestic insurance companies such benefits, as: expansion of the financial resource base, increase in the capitalization; increase in competition in insurance services, increased insurance density; growth of gross written premiums, increase of compensations and insurance indemnities paid etc. Also investigation revealed, that insurance companies with significant share of foreign capital, as institutional investors, prefer investments in Government securities and do not promote financing of real sector of economy and registered growth of investments in the capital market is influenced by the another factors then foreign investments in social capital of insurance companies (e.g. decrease in profit from investments in banks deposits etc.). Simultaneously, investigation of the international experience revealed, that on attraction of foreign investors in national insurance sector and on stimulation their activity as institutional investors in the capital market, influence such factors as*:* domestic and foreign political stability, economic growth, combination of fiscal and monetary stimulus, savings culture and financial education of individuals, demographic aspects, competition between capital market investments and substitute services such as bank-offered products, real estate investments etc., capital market depth and liquidity, modern and developed finance infrastructure, innovative trading and hedging mechanisms, wide variety of financial products in the capital market, transaction costs (commissions, fees and tax), human capital and professionalism, quality of regulation of the capital market, market surveillance and investor protection that must be taking into consideration of regulators in the Republic of Moldova in elaboration of the strategies of development of national financial market with scope of the attracting foreign investments and stimulation institutional investors activity in the capital market.

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