

THE FUTURE OF INVESTMENT DONE BY UNIT LINKED INSURANCE IN ROMANIA

Marius Gavriltea¹

¹Faculty of Business, Babs-Bolyai University, Cluj-Napoca, Romania
mgavriltea@yahoo.com

Abstract:

One of the most dynamic life insurance products in Romania is unit-linked insurance. The basis principles of this insurance are a combination between protection – insurance perspective, and capitalization - investment perspective. In the moment of buying such insurance, the potential client must choose an insured sum from a given interval, taking into account the individual appetite for protection or investment. During this paper, we will do an analysis of the evolution of this insurance for two major insurance companies in Romania, and a parallel research of the investment done by these insurance companies using the insurance life premiums. The accounts of the insured people are influenced by these investments, especially decreased by the worldwide financial crisis. In the end of the paper, we will present the conclusion and the proposal for both insurance companies and insured people.

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1. Introduction:

Unit linked insurance are life insurance policies with investment component. The insurance premiums are invested into one or more investment funds, managed by the insurance company. The investment is split into a share part named “unit”. Each investment fund has its’ own unit with individual prices. The insured persons choose the investments – the funds and the allocation between them. These funds are available only for the insured people of the insurance company. Each time the insured persons want, they must change the allocation of their investment.

In case of a traditional life insurance policy the investment risks are on insurance company - the insurance company will invest the money very carefully, especially in financial instruments with lower profitability – bonds, banking deposits. In case of unit- linked insurance policies the investment risks are on the insurance person’s side, but the benefits of the investment depend on the investment funds’ evolutions.

There can be separated the two components of the unit-linked insurance: *protection and investment*.

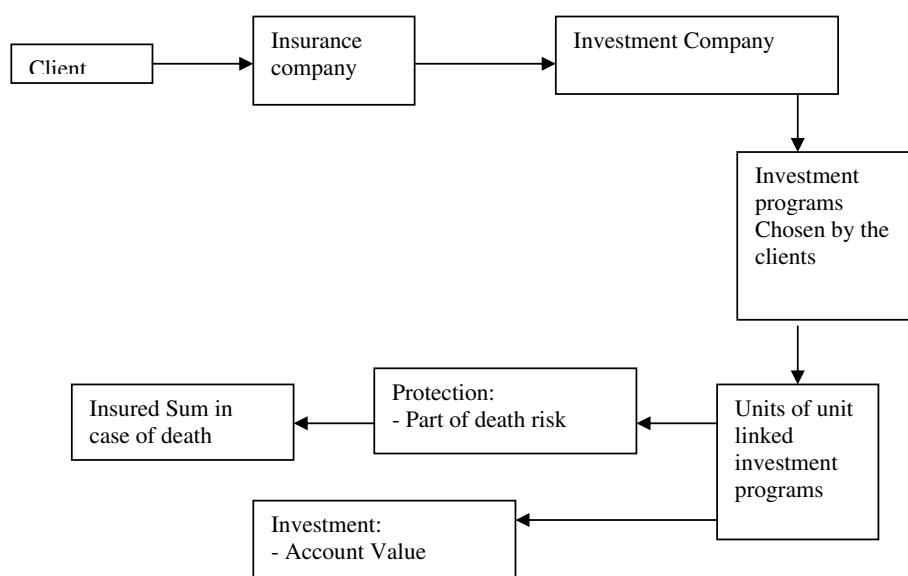
The protection part refers to the Insured Sum in case of death, and the investment one refers to the client's account. This account includes the present value of the units from the chosen investment funds.

2. Theoretical aspects:

Each investment program is divided in units, these units evaluate by the principle of equities and bonds on a regular stock exchange market.

The insurance premium has a simple circuit that is described in the next figure:

Fig.1. – Insurance premium circuit in case of unit linked life policies



The insurance companies allow the clients to pay extra insurance premiums if they want to modify the initial insurance contract. There can be two types of modification, for each part of the unit linked insurance:

- in case of protection, the clients may agree to introduce supplementary clauses for their health (surgery intervention, accidents, fracture intervention and others). In that case the supplementary insurance premiums are paid and if there is no risk occurred the money remains to the insurance companies
- in case of investment, the client may pay a supplementary premium that will entirely be allocated to the investment programs. These amounts are directly included into insured people's individual account, and will follow the investment principles

If we analyze the unit-linked insurance contracts, there are two situations when the insurance companies have financial obligations towards the insured persons.

In case of insured person' death the beneficiary persons will receive the maxim amount between the insured sum (mentioned in the policy) and the value of the individual account.

The other situation appears in the moment when the contract reaches the maturity and the person is alive. In this case the paid amount is the value of the individual account.

We can observe from these last phrases that the importance of the individual account is a huge one. But the value of the account depends on the investment programs of the insurance companies.

The insured people' thinking is very simple. They expect to receive more money than they paid during the contract period. The logic is a saving account from banking system. But they forget that in case of the insurance companies these are gathering the death risk, instead of banks that are not.

3. Research Methodology:

In these times when the financial crisis is an international problem, when all the international markets, investments funds, stock exchanges are down, the prices of the listed shares are very low, the life insurance companies are confronted with a delicate problem: the value of the accounts of the insured peoples. That is because the investments are done in financial quoted instruments.

The situation is very difficult especially for the persons that have theirs' contracts reached to maturity in this critical period. They find their account with less money than expected, less amounts than a year ago.

Beside this aspect, a lot of insured persons are afraid not to loose their value from the insurance policy account. They have a panic action, and they want to end the contract and to get back the account at this level (in expectation of a lower level).

In the next part of the paper we will analyze the existed situation in Romania for three big insurance companies (Allianz Tiriac, ING and AVIVA – former Commercial Union).

No matter the company is the programs enhance different types of financial instruments, diversified by the risk and profit. The insured persons choose the programs that suits well to theirs' attitude towards risk.

In case of Alianz Tiriac Life Insurance there are the following programs:

1. Conservator – the investments are done in Eur, especially in European bonds (75%) and shares of important companies (25%).

2. Clasic - the investments are done in Eur, especially in European bonds (50%) and shares of important companies (50%).

3. Progresiv - the investments are done in Eur, exclusive in shares of important European companies (100%).

4. Dinamic - the investments are done in Eur in European bonds (25%) and especially in shares of important companies (75%).

5. Euro-Plus - the investments are done in Eur, exclusive in bonds of important European governments (100%).

6. Dollar-Plus - the investments are done in USD, exclusive in bonds issued by US government (100%).

7. Leu-Extra – this program include 100 % savings and deposits in Romanian high solvency' banks (investment are done in national currency RON)

8. Leu-Plus –investment is done in RON and 100 % in treasury instrument with medium and long terms

Allianz Tiriace provide the availability of all data since the company enter in the life insurance market -2001.

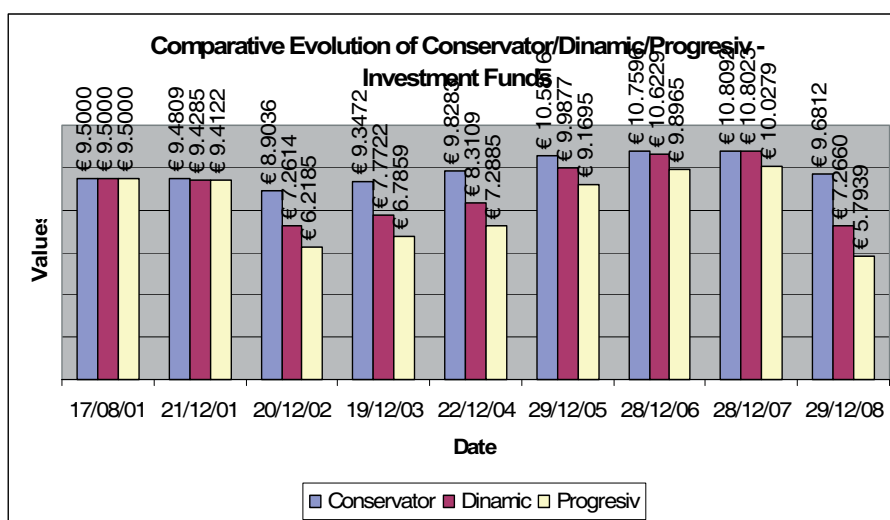
We observe that since 2001, 4 investment funds record a negative evolution, and the rest of 4 record a decent increase. The most risky funds (the ones within the investemnts are done especially in listed shares) with a huge risk apetite realized important decrease.The insured people that choose a lower risk program still may have more value in their account compared to the beginning.

Table 1. – Evolution of Allianz Tiriace investment funds 2001- 2008

Date m/y	Clasic (€)	Conser- vator(€)	Dinamic (€)	Dolar- Plus(€)	Euro- Plus(€)	Progresiv (€)	Leu-Extra (RON)	Leu-Plus (RON)
08/01	9.50	9.50	9.50	9.50	9.50	9.50	25.54	25.54
12/01	9.63	9.48	9.42	9.80	9.58	9.41	28.03	28.63
12/02	8.21	8.90	7.26	8.51	10.08	6.21	34.74	36.91
12/03	8.64	9.34	7.77	7.83	10.29	6.78	40.54	42.50
12/04	9.17	9.82	8.31	7.48	10.80	7.28	47.23	49.24
12/05	10.39	10.58	9.98	8.38	11.01	9.16	52.69	54.54
12/06	10.79	10.75	10.62	7.76	10.74	9.89	55.90	56.80
12/07	10.90	10.80	10.80	7.06	10.60	10.02	59.03	59.26
12/08	8.54	9.68	7.26	6.78	11.13	5.79	65.05	65.56

We observe that in the last year – 2008, only 3 funds recorded a increase: Euro Plus (Eur) of 5% and Leu-Extra/Plus of 10.6%. The rest of 5 funds recorded a decrease; the most important one is of 42.3% for Progresiv (Eur). In the next graphic we present the evolution of three funds, from the start to the end of 2008. The one that choose Conservator program has almost the same value, and the people that choose Dinamic and Progressive programs (the most risky of all) recorded substantial losses in the accounts.

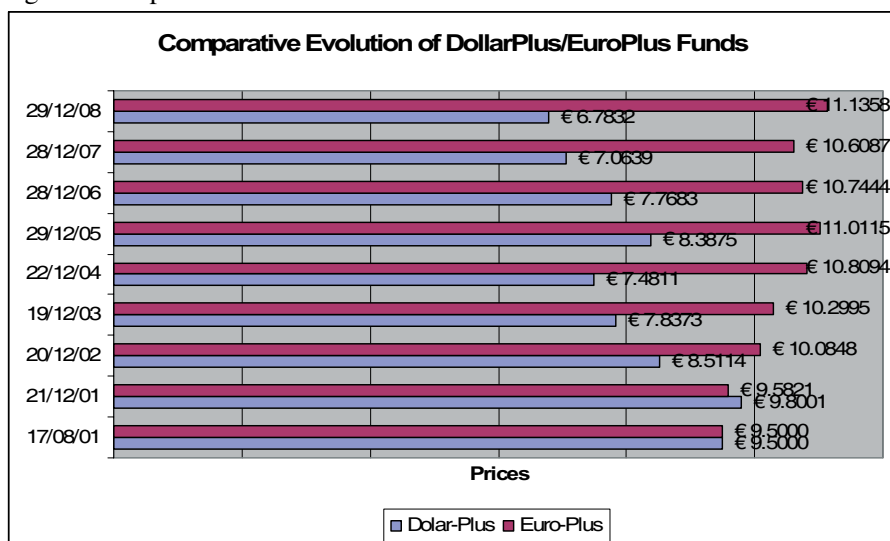
Fig.2. – Comparative Evolution of Conservator/Dinamic/Progresin Funds



Also, we notice the Progressive Fund, recorded the highest depreciation, from starting value of 9.50 Euro to 5.79 Euro.

The evolution of other two funds Dollar Plus and Euro plus are described in the next graphic:

Fig.3. – Comparative Evolution of Dollar Plus/Euro Plus Funds



We notice that even if Dollar Plus and Euro Plus seem to have a similar risk (the investment are done exclusive in bonds), the practice trend show us that Dollar Plus recorded a continuous depreciation, and opposite Euro Plus a constant increasing. This fact may be generated by the evolution of US economy – USD depreciation towards other international devices, the starting of the world crisis was in US.

AVIVA Life insurance company has the following investment funds:

1. Capital Garantat is an investment fund with 100% safe portfolio, in state bonds and deposits on the prestigious Romanian banks.

2. Practic 25 (Plus) is a medium risk investment fund, with a structure made of 25% Bucharest Stock Exchange listed shares and 75% of local, govern and national companies bonds.

3. Practic 50 (Max) is a higher risk program where investment in BSE listed companies is up to 50% and the rest of 50% represents the bonds.

Beside the local funds (RON currency) there are other funds with international currencies - USD and EUR.

4. Suprem is a highly randament program, which include a portfolio of 70% in strong international companies and 30% bonds issued by different governments. The risk level of the program is a high one.

5. Actual is a medium risk investment fund with 100% investments in bonds issued by European corporations.

6. Median is also a medium risk program, the investments are done 70% in international governmental bonds and 30% in international corporations' bonds.

7. Conservator allows the investments into a group of governmental bonds, with a low level of risk.

8. Imobilis offers direct investments on the real estate markets in Central and Eastern Europe, the risk is a medium – high one.

Evolution of the investment programs in AVIVA case is described in the next figure – but we must mention that there were no available data from other years than 2007 and 2008.

Table.2. – Price Evolution 2008/2007 for AVIVA Investment Funds

Investment Fund	Price (Dec. 2008)	Price evolution in the last year (2008/2007)
Capital Garantat (RON)	3.54	9.64%
Practic 25 – RON	1.20	-16.19%
Practic 50 – RON	0.78	-36.01%
Suprem –USD	0.82	-33.23%
Median – USD	1.17	-17.13%
Conservator - USD	1.43	-4.78%
Actual – USD	1.49	-19.60%
Imobilis – USD	0.70	-43.48%

Suprem –EUR	0.27	-26.91%
Median – EUR	0.38	-9.93%
Conservator – EUR	0.41	3.28%
Actual – EUR	1.07	-12.83%
Imobilis – EUR	0.62	-38.74%

In case of Aviva only 2 funds recorded increasing in 2008, and the others decreased, the most important decrease was recorded in case of Imobilis funds with 43.48%.

One fund that increase is in RON (9.64%) and the other is in EUR (3.28%) these have a minim risk because of its instrument.

The depreciation in the other funds is normal, the stock exchanges recorded depreciation worldwide and also the real estate industry (Imobilis). Because of the prices' collapses in the real estate industry in Romania, Imobilis fund recorded that negative evolution.

Investment programs in case of ING Life Insurance are six; two of them use Romanian currency – RON, and the rest use USD for units' quotations. These funds have the following characteristics:

1. Bond – investment are exclusively in RON, 100% in monetary instruments from the Romanian financial market.

2. Mixt25 - investment are in RON, 75% in monetary instruments from the Romanian financial market and 25% in shares of important Romanian companies listed on Bucharest Stock Exchange.

3. White – investments are done in USD, 10% of them in monetary international instruments with 1 year maturity, 60% in medium time bonds issued by OECD or European countries, 30% in shares quoted on international stock exchanges

4. Blue - investments are done in USD, 20% of them in monetary international instruments with 1 year maturity, 70% in medium time bonds issued by OECD or European countries, 10% in shares quoted on international stock exchanges

5. Red – investments are done in USD, 30% in medium time bonds issued by OECD or European countries, 70% in shares quoted on international stock exchanges

6. Green - 100% in monetary instruments from the Romanian financial market, international markets – all of them in USD.

In the next table we gathered the prices of the units since 2001 (the funds were active since 1998 when ING launched unit linked insurance in Romania), in order to have a real comparing with Allianz.

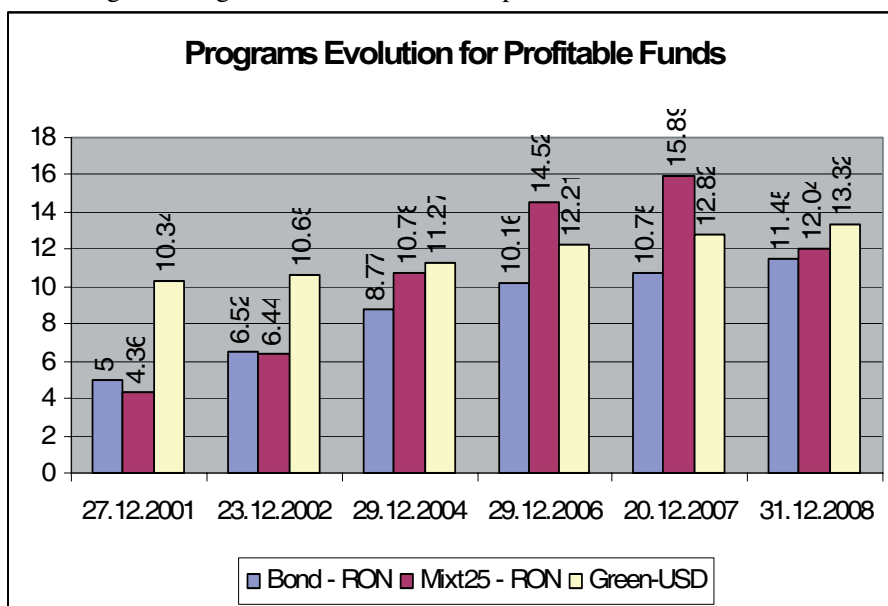
Table 3. – Evolution of ING Romania Investment funds 2001- 2008

Investment Funds / Date	27.12.2001	23.12.2002	29.12.2004	29.12.2006	20.12.2007	31.12.2008
Bond - RON	5.00	6.52	8.77	10.16	10.75	11.45
Mixt25 - RON	4.36	6.44	10.78	14.52	15.89	12.04
Green-USD	10.34	10.65	11.27	12.21	12.82	13.32
Red-USD	7.89	6.97	9.52	11.09	11.61	7.48
White-USD	9.01	9.19	12.13	12.86	13.67	10.93
Blue-USD	9.37	10.17	13.12	13.27	14.24	13.43

From this table we notice that the two funds in RON recorded increases in the analyzed period and also Green fund in USD. The last fund' evolution is a logical one because been formed by guaranteed monetary instruments is a low risk fund.

The profitability is from 2001, even if in the last year 2008 one fund from the last three mentioned recorded a decrease.

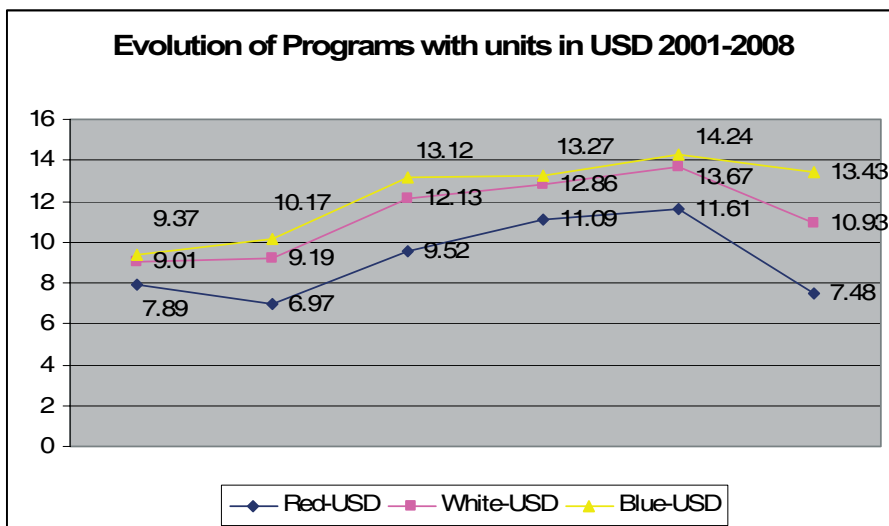
Fig.4. – Programs evolution for ING profitable funds



In case of these profitable funds the prudentially investment make the increase to be a low and a constant one.

The funds that invest the money in listed companies' shares, recorded a decrease especially in the last year. Of course the clients that choose to invest in these medium and high risky programs have less money in theirs' accounts.

Fig.5. – Programs evolution for ING funds with units in USD

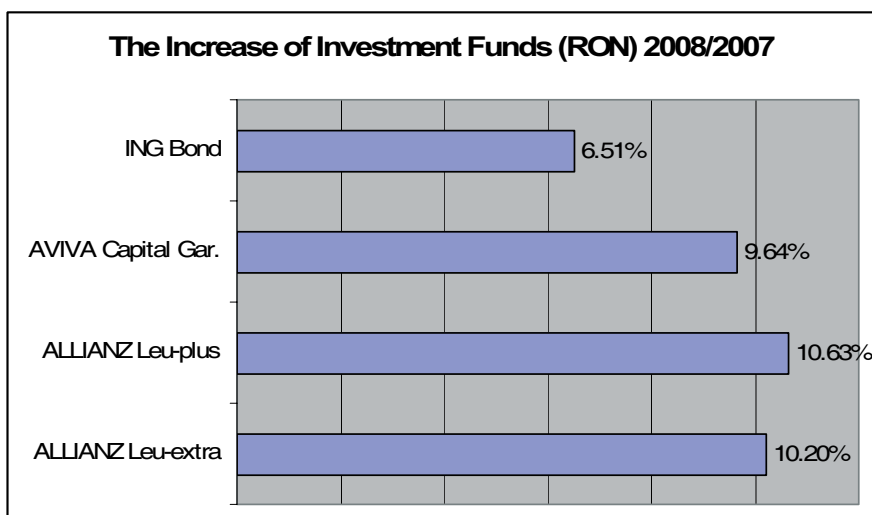


Red investment fund recorded the worst decrease in 2008 – 35.5%. This is why the fund is the most exposed one; investments are done preponderant in listed shares.

After analyzing this three life insurance companies we observe that even if the crisis predominate in the financial markets, the managers of the investment funds proved theirs' professionalism and in the last year got profit. The profitable investment funds are the one in Romanian currency and the ones with a high percentage of investment in monetary instruments, bonds guaranteed by different Governments.

We compare in the next graphic the increase in the last year of the investment funds with Romanian currency:

Fig.6. – The increase of investment funds in 2008/2007



Allianz Tiriac Life Insurance recorded the highest increase of 10%. But we must take into account the medium level of inflation in 2008 of 7.85%. That means that only AVIVA and Allianz recorded a real profit.

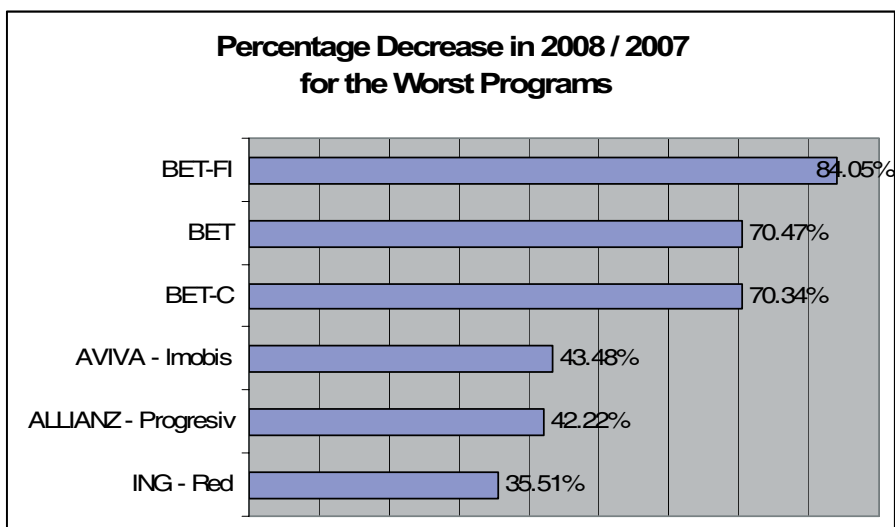
4. Conclusions:

The life insurance companies in Romania find themselves into a delicate situation, the way they will manage this period, will influence the future of their prestige and not in the end the clients account.

If we compare the investment funds with the worst evolution together with the indexes of Bucharest Stock Exchange we will notice that the depreciation is not so high.

The evolution of BSE indexes in 2008 was a negative one: BET recorded a decrease of 70.47%, BET-C a decrease of 70.34%, BET-FI 84.05%, ROT-X 69.64%, BET-XT 76.26% AND BET-NG 72.31%.

Fig.7. – Percentage decrease
in case of insurance investment funds compared to BSE indexes
2008/2007



The “worst” depreciations of the investment funds are less than the correction in the listed shares. This happened because the insurance companies when launched the programs avoided investing all the funds 100% in shares.

Therefore, the evolution of the insurance companies investment funds must be explained to the clients comparing to financial markets evolutions, in that situation the insured people will understand that insurance companies managed in the best way investors’ money.

Moreover, the financial consultants of the life insurance companies should explain the present option: to redirect the money from the less profitable investment funds to the profitable ones. And in the moment they consider that the depreciation trends in the international markets ended, they must choose again the medium or high risky investment programs.

We would like to mention that the accounts’ situation may not be as negative as the investment funds show us. This may be explained by at least two mentions:

- the greatest number of the insured people have chosen to invest their insurance premium in more than one investment fund, so the risk is already spread from the beginning of the policy
- some of the clients already change the units allocation during the last year at the moment when the financial markets confirmed the depreciation trend

Also, the reimbursement of the actual account of some clients must be well explained. In the moment a client choose to end the contract before the maturity, there will be some penalties taxes from the insurance company and the effective received money are even less.

The cycle of the financial market is an economical situation, and the period is not a long one. The persons that have long time insurance policies should be patient because in a policy time the increasing and decreasing are inevitable.

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