

The Insurance Industry in Mauritius

Dimitri Vittas

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Abstract

The insurance industry is relatively well developed. It makes extensive use of reinsurance facilities and is free from the pervasive premium, product, investment, and reinsurance controls that have bedeviled the insurance markets of so many developing countries around the world.

Total premiums amounted in 2001 to 4.1 percent of GDP, while insurance company assets were equivalent to 18 percent of GDP.

Life insurance, which has been favored by generous tax incentives and has also benefited from the growth of pension business and housing finance, represents 61 percent of total premiums.

Nonlife business is also well organized. Large industrial and commercial risks are reinsured with top international companies, while motor insurance, which is the largest class of business with 45 percent of total nonlife premiums, does not suffer from high loss ratios or unduly long delays in settlement.

Investment limits are generally sound and, with some small but important exceptions, effectively nonbinding. There is no minimum requirement for investment in government securities. Investment in overseas assets is limited to 25 percent of total assets, except for foreign life companies and general insurance business which are not allowed to invest in overseas assets.

The insurance sector is highly concentrated. The three largest groups have 76 percent of total assets. Despite the high level of concentration, the insurance industry appears to be competitive, operating with high efficiency and reasonable profitability.

Large and medium-size companies have strong reserves, appropriate reinsurance arrangements, and good profitability. However, several of the smaller companies have weak financial ratios and suffer from long delays in settling claims.

Insurance regulation and supervision is entrusted to the Financial Services Commission (FSC). The current regulatory framework has many strong elements, including reliance on solvency monitoring, prudent asset diversification, international accounting standards, and actuarial methods.

But there are some important gaps in corporate governance, internal controls, and risk management. In addition, solvency ratios are below international standards and do not include modern risk-based capital requirements. These gaps are already being addressed in two new draft insurance bills which contain many highly modern provisions. Implementing regulations on solvency and actuarial standards need to be developed.

Insurance supervision has been invigorated since the creation of the FSC, but further strengthening is required. It needs to emphasize risk management and internal controls, to develop an early warning system, and to establish clear procedures for early and effective intervention.

The FSC should require actuaries to report on the reinvestment risk faced by insurance companies and their exposure to a large and persistent fall in interest rates.

This paper—a product of the Financial Sector Operations and Policy Department—is part of a larger effort in the department to study insurance companies and contractual savings. Copies of the paper are available free from the World Bank, 1818 H Street NW, Washington, DC 20433. Please contact Priscilla Infante, room MC9-904, telephone 202-473-7642, fax 202-522-7105, email address pinfante@worldbank.org. Policy Research Working Papers are also posted on the Web at <http://econ.worldbank.org>. The author may be contacted at dvittas@worldbank.org. April 2003. (19 pages)

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**Financial Sector Development
World Bank**

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Glossary

FSC	Financial Services Commission
IBNR	Incurred But Not Reported
NEP	Net Earned Premiums
NIC	Net Incurred Claims
NPF	National Pensions Fund
NSF	National Savings Fund
ROA	Return on Assets
ROE	Return on Equity
SICOM	State Insurance Corporation of Mauritius

I. Introduction

Mauritius, a small island economy in the Indian Ocean off the coast of Africa, has been remarkably successful in achieving rapid economic growth in the context of financial and political stability. This success is in sharp contrast to the poor economic performance of most neighboring countries in the African continent and has been attributed to the pursuit of stable macroeconomic policies and the creation of a regulatory framework that encourages private sector development. The importance of efficient and well functioning institutions in explaining the strong growth performance of Mauritius is highlighted in Subramanian and Roy (2001).

These policies have benefited many sectors of the economy, including the financial sector. They have stimulated the growth of banks as well as insurance companies and pension funds. The authorities have avoided using price and product controls and imposing prescribed investment requirements on financial institutions. Instead of relying on direct controls, they have placed greater emphasis on applying sound prudential regulations to ensure that financial institutions are able to compete and innovate without undermining the security of the financial savings of the public.

This paper examines the structure and performance of the insurance industry in Mauritius.¹ The Mauritian insurance industry is relatively well developed, makes extensive use of reinsurance facilities, and is free from the pervasive premium, product, investment and reinsurance controls that have bedeviled the insurance markets of so many developing countries around the world. The paper aims to document the success of the insurance sector, but also to highlight some important areas where problems arise. In particular, the need for a more effective supervision of insurance companies is stressed.²

The paper is organized as follows. Section II reviews the extent of insurance market development in comparison to other countries. Section III focuses on its institutional structure and overall performance. The following three sections offer in turn brief reviews of the state of development, structure and performance of long-term (life), general and motor insurance. Section VII examines the regulatory and supervisory framework, drawing attention to its strengths and weaknesses. The paper concludes with a section on future prospects and policy issues.

II. Insurance Market Development

Mauritius has a much higher insurance penetration (premiums as a percentage of GDP) than India, Lebanon, Morocco and Sri Lanka and is on the same level as Chile, Cyprus and Singapore (Sigma 2002). Total annual premiums amounted to 5.3 billion rupees in 2001, corresponding to 4.1 percent of GDP (Table 1). Life premiums

¹ Similar analyses have been undertaken for the US insurance industry by Wright (1992) and Grace and Barth (1993) and for Tunisia by Vitas (1995).

² The paper does not cover the operations of the captive insurance companies or the Sugar Insurance Fund that offers specialized coverage to sugar planters and millers.

represented 61 percent of the total, providing a further indication of the development of the sector. The level of per capita premiums amounted to USD 156 in 2001. This compared with USD 12 in India, 10 in Sri Lanka and 113 in Mexico.

Table 1: Insurance Premiums, 2001
percent of GDP Total Non-Life Life % Life

Mauritius	4.06	1.59	2.47	61
Chile	4.23	1.30	2.93	69
Cyprus	4.46	2.00	2.46	55
India	2.71	0.56	2.15	79
Hong Kong	6.34	1.21	5.13	81
Lebanon	2.70	2.22	0.48	18
Malaysia	5.18	1.80	3.38	65
Malta	4.26	2.28	1.99	47
Mexico	1.81	0.95	0.86	48
Morocco	2.82	2.01	0.81	29
Singapore	4.58	1.17	3.40	74
South Africa	17.97	2.78	15.19	85
Sri Lanka	1.20	0.67	0.53	44

Source: FSC and Sigma.

Life business has been favored by generous tax incentives and has also benefited from the high level of development of pension funds on the one hand and housing finance on the other (Vittas 2003). In recent years, life insurance business and the total assets of insurance companies, which are linked to life policies, have grown faster or, at least, as fast as GDP (Table 2). The share of life premiums in total insurance premiums has been rising steadily.

The breadth of tax incentives cannot be exaggerated. Life premiums are deductible from income tax up to MUR 80,000 per family per year (about 80 percent of per capita income), while investment income is treated favorably and policy payouts are free from tax. In addition, both pension saving and housing loans enjoy considerable tax advantages. Pension contributions are exempt from tax without any ceiling, while interest on housing loans is deductible up to MUR 250,000 per family per year. Interest relief is available on all secured loans used for primary housing or education purposes, even those secured by life insurance policies – thus providing a further incentive for purchasing life insurance to middle and high income people.

Table 2: Evolution of Insurance Business, 1997-2001

	1997	1998	1999	2000	2001
	(percent of GDP)				
Total Assets	16.0	16.7	17.9	17.8	18.2
Life Premiums	2.15	2.16	2.21	2.34	2.47
General Insurance Premiums	2.07	1.81	1.68	1.66	1.59
Total Gross Premiums	4.22	3.97	3.89	4.00	4.06
Share of Life Business (%)	51	54	57	58	61

Source: FSC

Internationally, South Africa and Ireland have very large life insurance sectors and in both countries, tax incentives play a major part that is fuelled by the high marginal tax rates applying in these countries. In Mauritius, the relatively low personal income tax rates and the availability of a large variety of deductions weaken the tax advantages of individual life insurance policies.

In the nonlife sector, motor insurance is the largest component. It does not suffer from very high loss ratios as is the case in most other developing countries. The use of high deductibles has helped to keep loss ratios low and has allowed many small insurers to survive despite their operating inefficiencies. General insurance business is subject to high volatility of premiums, claims and earnings linked to cyclical fluctuations in economic activity and the adverse impact of large losses caused by low frequency events, such as devastating cyclones and fires affecting large textile factories and hotels. Insurance companies use international reinsurance facilities for their large industrial and commercial risks. Most companies are well capitalized and reserved, although some small companies have long faced financial difficulties.

Insurance companies are major participants in the contractual savings market. As noted in Vittas (2003), Mauritius belongs to a select group of developing countries where contractual savings (i.e., savings with insurance companies and pension funds) exceed 40 percent of GDP and represent a major potential force in the local financial system.

Other developing countries with large contractual savings sectors include South Africa, Malaysia and Chile alongside most high income countries and some island economies like Cyprus and Malta. The vast majority of developing countries in Africa, Asia and Latin America as well as most transition countries of Eastern Europe are well below this level.

The total assets of insurance companies from both their pension and non-pension business amounted in 2001 to MUR 24 billion, equivalent to 18.2 percent of GDP. This represented 45 percent of net contractual savings. Nearly 40 percent of insurance company assets are linked to pension schemes that are insured and/or administered by insurance companies.

The other major participants in the contractual savings market are the National Pensions Fund (NPF) and National Savings Fund (NSF), which have a combined 45 percent of the market, and the self-administered funded pension schemes created by statutory bodies and private companies, which account for the remaining 10 percent. Public sector institutions, including the NPF, NSF and the State Insurance Corporation of Mauritius (SICOM) are responsible for managing 57 percent of the total, although the operations of SICOM are no different from those of any private sector manager.

As a group, contractual savings institutions invest heavily in government securities (mostly two-year treasury bills) and housing loans. But since they benefit from positive cash flows and their total assets are likely to continue to grow relative to GDP, they represent a major source of demand for long-duration assets. They can therefore stimulate the development of the market for long-term government bonds (both inflation-

linked and zero-coupon), corporate debentures, mortgage bonds and mortgage-backed securities, corporate equities, and venture capital.

III. Institutional Structure and Performance

There are 22 insurance companies operating in Mauritius.³ This is a large number for the size of the local market, although some of the smaller companies appear to serve segments of the market that are unattractive to the larger companies. 19 of these companies are locally incorporated by Mauritian interests, 2 are local branches of Indian companies (present in Mauritius since the early 1960s), and the last is the South African subsidiary of Munich Re, which specializes in reinsurance.

11 of the 19 local companies operate as composites, engaging in both life and nonlife business, while 2 specialize in long-term (life) business and 6 in short-term (general) insurance. Two groups operate separate insurance subsidiaries in both segments of the market. One of the Indian companies is a long-term insurer, while the other specializes in short-term business.

The insurance industry experienced considerable new entry over the past two decades. 5 new companies were established in the 1990s and another 5 in the 1980s. Several of these companies face financial difficulties, including 3 that were intervened over the past couple of years. The authorities have raised the minimum capital requirement (now standing at MUR 25 million, close to USD 1 million) in an attempt to strengthen the financial soundness of all companies and encourage a consolidation of the sector through mergers, but so far there has been very limited exit through merger or liquidation.

Some of the smaller companies incurred large losses over several years. In one case, accumulated losses exceeded the paid up capital of the company, resulting in the company operating with negative equity. Another 2 companies had equity capital significantly below the minimum capital requirement. All these companies received capital injections during 2002.

Foreign companies may operate with branches or subsidiaries. Apart from the two Indian companies, and the recent arrival of a Sri Lankan company, there are no other foreign companies. None of the large multinationals has a local presence in Mauritius, perhaps because of the small size of the market and the strong performance of local companies. However, one multinational company has a small stake in a medium size local company.⁴

Despite the presence of a large number of companies, the sector is characterized by a highly oligopolistic structure with a few companies holding the lion's share of the market. However, the market is deemed to be contestable with keen competition in several segments. The largest three groups (SICOM, Swan/Anglo Mauritius, and British American Insurance) control 76 percent of total assets. The largest company is effectively

³ Another 2 companies are registered but are not active.

⁴ Eagle Star of South Africa of the Zurich Group has a participation in Mauritian Eagle.

owned by the state, either directly or through other state entities. Nevertheless, it appears to operate at arm's length from the government and to be highly efficient and profitable. It has a 36 percent share of total insurance company assets, but this includes the assets of pension funds, mostly of statutory bodies, that it administers but does not insure. Excluding this business, its share of total assets falls to 11 percent.

Dividing the 21 insurance companies by size reveals some interesting patterns (Table 3)⁵. The four largest companies account for 76 percent of total assets, but 84 percent of retained profits, while small companies account for only 3 percent of the market. The 8 small companies as a group have negative accumulated (retained) profits, but they report as a group high solvency ratios. However, some of the small companies have strong balance sheets and sound operations.

Table 3: Structure and Performance of Total Insurance Market, 2001

(percent)	4 Large Companies	9 Medium Companies	8 Small Companies	1 Reinsurer	All Companies
Total Assets	75.7	20.7	2.9	0.6	100.0
Equity Capital	61.8	31.1	7.1		100.0
Retained Profits	83.8	21.2	-7.9	2.9	100.0
Gross Premiums	59.7	31.9	8.3	0.1	100.0
Equity/Total Assets	7.86	14.44	23.47		9.69
Equity/Total Premiums	44.8	42.1	37.5		43.3
Return On Average Equity	21.5	20.9	13.3		20.7
Return on Average Assets	1.73	2.93	2.94		2.00
Profits/Gross Premiums	9.18	8.16	4.62		8.48

ROE and ROA are equal to profits before taxes divided respectively by average equity and average assets.

Source: Estimated on the basis of data collected by the FSC..

Profitability of the insurance sector is healthy, but not excessive, despite the high level of concentration of the industry. This supports the argument that the market is contestable. The return on average equity (ROE) amounted to 21 percent for all companies taken together in 2001, but was significantly lower for the group of small companies. The return on average assets (ROA) amounted to 2 percent. It was lower for the large companies, because of their lower equity ratios and reached nearly 3 percent for the other groups of companies. A couple of individual companies report very high ROAs of well over 4 percent. These companies operate with very high equity ratios. In one case, equity capital exceeds 40 percent of total assets.

The insurance industry suffers from considerable cyclicalities (Table 4). In Mauritius this is linked to the impact of cyclones and other causes of large but infrequent losses. Judicious use of reinsurance facilities has, however, shielded local companies from the full effects of such events. Cyclicalities are also linked to the conditions that prevail in financial markets. While the level of interest rates in Mauritius has not experienced the wide fluctuations that are seen in other countries, financial results have suffered from the volatility of local and international equity markets. Insurance

⁵ The reported data aggregate statistics of individual companies. Most companies have financial years ending in December but several report at the end of June and some use other months.

profitability was low, though still satisfactory, in 1999 as a result of the effects of protracted drought.

Table 4: Cyclicalities of Financial results, 1997-2001

	1997	1998	1999	2000	2001
Own Funds/Total Liabilities %	10.7	10.4	10.0	9.5	9.7
LT Insur Fund/Total Liabilities %	72.3	73.3	75.7	76.9	77.6
General Insur Reserves/Total Liabilities %	7.6	6.8	6.1	5.7	5.2
ROA	2.19	2.02	1.54	1.61	2.00
ROE	20.6	19.4	15.4	17.0	20.7
Profits/Gross Premiums (%)	8.33	8.50	6.87	7.18	8.48

Source: FSC

Insurance companies have adequate asset diversification. According to FSC statistics, government securities represented 8 percent of total assets and corporate securities (both equities and debentures) 35 percent (Table 5).⁶ Housing loans account for 23 percent of assets. They used to be the largest type of asset but have declined in recent years, reflecting the growing presence of banks in this important market. Although the long-term insurance fund, representing the assets of life business, can be invested overseas up to a limit of 25 percent and despite the presence of several large privately owned companies, foreign securities absorb less than 10 percent of total assets. In fact, SICOM, the state-owned company, invests more in foreign assets than even the large private companies. Other assets absorb 11 percent of total assets. They include loans to shareholders, which in the case of some small companies, are large relative to capital (see below).

Table 5: Asset Allocation of Insurance Companies, 1997-2001
(percent of total)

	1997	1998	1999	2000	2001
Mortgage Loans	30	26	25	25	23
Other Loans	8	5	5	5	4
Government Securities	7	9	6	7	8
Shares & Debentures	22	26	30	35	35
Land & Property	6	7	6	5	5
Deposits & Securities	16	16	17	13	14
Other Assets	11	11	11	10	11
Total	100	100	100	100	100
Total Assets (MUR million)	14130	16672	19200	21123	23971

Source: FSC

IV. Long-Term (Life) Insurance

14 companies operate in the life sector. 11 of these are composites and only 3 specialize in life insurance (2 Mauritian companies plus the local branch of the Life Insurance Corporation of India). Concentration in the sector is very high. The largest 3

⁶ As noted above, official statistics probably understate the share of government securities in the portfolios of insurance companies.

companies accounted for 79 percent of premiums in 2001, while the Herfindahl concentration index stood at 2168. Concentration is even higher with regard to the long term insurance fund. The share of the long term fund held by the largest 3 companies was 83 percent, while the Herfindahl index was as high as 2872.⁷

Despite the high level of concentration, it is claimed by local experts that competition for new business is very keen. The largest 3 companies specialize in particular segments of the market that they dominate. SICOM obtains a very large part of its business from the pension funds of statutory bodies, while Anglo-Mauritius has a dominant share of insured company pension schemes. British American specializes in what looks like "industrial life" insurance: low-premium, low-value insurance sold to low-income households. In fact, British American has 60 percent of premiums generated by new business, although it probably experiences much higher lapse and surrender rates than the other large companies. Allowing for these differences, competition for new business in other market segments is much keener than may be implied by the overall concentration indices.

Long-term insurance business operates on the whole with sound financial ratios (Table 6). A small part of premiums is ceded to reinsurers (4 percent), while net claims (payments for all kinds of benefits, including surrenders) amount on average to 52 percent of net premiums. Administration costs absorb about 17 percent of net premiums and net commission paid to agents add another 4 percent, resulting in a total charge of 21 percent of net premiums.

Table 6: Financial Ratios of Long-Term Insurance, 1997-2001
(percent)

	1997	1998	1999	2000	2001
Ceded Premiums/Gross Premiums	5.3	4.1	4.1	4.2	3.8
Net Claims/Net Premiums	48.2	54.6	54.2	52.8	52.5
Net Commissions/Net Premiums	6.1	5.4	4.6	4.3	4.0
Admin Costs/Net Premiums	15.3	16.1	15.9	16.6	16.8
Investment Income/Net Premiums	56.9	72.5	63.2	58.4	52.7
Annual Surplus/Net Premiums	90.0	96.4	88.5	84.7	79.4
Change in Life Fund/Net Prem	91.4	93.2	86.0	80.8	75.2
Profit/Net Premiums	-1.4	3.2	2.5	3.9	4.2
Profit/Annual Surplus	-1.6	3.4	2.8	4.5	5.3
Return on Average Life Fund	10.9	13.4	10.9	10.2	9.5

Source: Estimated on the basis of data collected by the FSC.

Investment income on the life fund has fluctuated significantly over the years reflecting market returns on the underlying assets. On average it amounted to around 60 percent of net income, leaving an annual surplus in excess of between 80 and 95 percent of net premiums. Over 95 percent of the annual surplus has been credited to the life fund.

The rate of return on the life insurance fund has fluctuated between 9.5 and 13.4 percent between 1997 and 2000. This is at the same level as that achieved by the National

⁷ In the US, a Herfindahl index of 1800 is used as a threshold value for defining a market as concentrated and meriting the attention of competition policy authorities.

Pensions Fund and compares favorably with the performance of self-administered private pension funds (Vittas 2003).

Reserving policies are deemed by local actuaries to be adequate, at least for the large and medium companies. Actuaries use mortality tables from the United Kingdom, while future actuarial liabilities are discounted at nominal rates that are close to prevailing market interest rates.

The typical life policies are participating policies where 90 percent of profits must be distributed to policy holders. Unit-linked business is not well-developed. Housing loans are tied to endowment insurance, though borrowers may opt for life cover on a declining balance basis.

The more advanced companies adopt modern asset/liability management techniques in determining the allocation of assets. However, the absence of zero coupon bonds and other sophisticated instruments and the general underdevelopment of the local financial markets limit the applicability of such techniques.

The life insurance companies face considerable reinvestment risk arising from the current duration mismatch of their assets and liabilities. This is caused by the dearth of long-term assets in the local financial system on the one hand and the prevalence of long duration liabilities on the other. Some insurance companies offer minimum guaranteed rates of return on their policies, but these are subject to periodic review, thus limiting the exposure of insurers to a large and persistent fall in the level of interest rates. Guaranteed rates of return are low compared to the current level of interest rates and insurance companies typically retain considerable discretion over terms and conditions. Nevertheless, insurance companies in several European countries have been hit by the offer of guaranteed returns and caution is advisable.

Endowment insurance policies are linked to housing loans and thus are nominally well hedged. But they raise the possibility of even greater mismatch exposure if housing loans were prepaid in the event of a large fall in interest rates, but endowment policies were not surrendered. Admittedly, companies have built in various protective features in their operations but could still be exposed to large losses. Similarly, group pension business that is linked to defined benefit plans involves the offer of guaranteed annuity options that could expose insurance companies to significant losses in the event of a large and persistent fall in interest rates.

Operating and investment performance varies considerably among individual companies by size. In general, the 3 largest companies operate with much lower administration and acquisition costs of 21 percent of net premiums against a hefty 41 percent for small companies (Table 7). Large companies earned in 2001 (as well as in some earlier years) a lower return on their life insurance fund than the smaller companies. However, the difference in returns was small and was completely offset by the higher administration and acquisition costs of smaller companies. The higher level of claims of small companies, probably reflecting a greater occurrence of policy surrenders, and their

higher expense ratios resulted in a much lower annual surplus and a slower build-up of the life fund.

Table 7: Structure of Long-Term Insurance, 2001

(percent)	3 Large Companies	5 Medium Companies	6 Small Companies	All Companies
Gross Premiums	79.0	17.7	3.3	100.0
Ceded Premiums/Gross Premiums	3.2	5.7	8.8	3.8
Net Claims/Net Premiums	53.1	48.2	60.2	52.5
Net Commissions/Net Premiums	3.2	6.9	8.4	4.0
Admin Costs/Net Premiums	14.4	20.6	32.7	16.8
Investment Income/Net Premiums	53.4	49.8	51.8	52.7
Annual Surplus/Net Premiums	82.7	74.1	50.6	79.4
Change in Life Fund/Net Premiums	82.5	69.2	42.6	75.2
Return on Life Fund	10.2	10.4	11.1	9.5
Multiple of Assets over Premiums	6.2	4.8	4.0	5.9

* percent of gross premiums

Source: Estimated on the basis of data collected by the FSC.

V. General Insurance

18 companies operate in the general insurance market, 11 are composites and 7 specialize in nonlife business. However, one of the composites (British American) is predominantly a life insurer with a very small and selective participation in nonlife insurance. The general insurance market comprises five classes of business, viz. fire, motor, personal accident, transport and miscellaneous. Except for the last named, concentration is much smaller in these classes than in life insurance. For general insurance as a whole, the four largest companies accounted in 2001 for 56 percent of gross premiums, while the Herfindahl index amounted to 1090 (compared with 2168 for life insurance).

Motor insurance is the largest class of general insurance, accounting for 45 percent of total nonlife premiums in 2001 (Table 8). Its share has been rising, reflecting the growing number of cars in circulation. But the fire and miscellaneous insurance classes are also relatively large, each with about 20 percent of total premiums. These two lines cover large industrial and commercial risks and tend to rely heavily on reinsurance.

Most large industrial and commercial risks are reinsured with nonproportional treaties. This is a very sound policy, because their gross claims ratios show considerable variability, connected to the volatility of large losses caused by low frequency events. Outside motor insurance, where only 13 percent of premiums are ceded to reinsurers, the other four classes operate with an average reinsurance ratio of 75 percent. In line with most developing countries around the world, product liability and malpractice insurance are not developed.

Table 8: General Insurance by Line of Business, 1997-2001

	1997	1998	1999	2000	2001
Gross Premiums					
	(percent of total premiums)				
Fire Premiums	26.2	22.8	22.6	20.2	20.4
Motor	37.9	41.4	41.9	43.6	44.5
Personal Accident	8.8	7.6	7.9	7.5	7.8
Transport	9.4	9.4	8.3	7.8	9.3
Miscellaneous	17.7	18.8	19.5	20.8	18.0
Total	100.0	100.0	100.0	100.0	100.0
Reinsurance Ratio					
	(percent of gross premiums)				
Fire	79	80	84	85	85
Motor	15	13	14	14	13
Personal Accident	57	65	68	68	70
Transport	62	61	61	60	62
Miscellaneous	65	68	67	76	70
Total	49	47	48	49	47
Gross Claims Ratio					
	(percent of gross premiums)				
Fire	33	33	242	30	24
Motor	64	78	81	86	74
Personal Accident	41	42	39	32	32
Transport	20	36	38	21	24
Miscellaneous	47	55	94	79	62
Total	47	57	113	59	53
Net Claims Ratio					
	(percent of net premiums)				
Fire	29	41	100	36	34
Motor	66	71	77	74	65
Personal Accident	49	38	48	32	43
Transport	28	39	34	23	31
Miscellaneous	45	58	75	68	62
Total	56	63	75	66	59

This table follows the classification used by the FSC. Reinsurance treaties are placed according to fire (including flood and cyclone); engineering (including contractors all risk and machinery breakdown); marine (including cargo, hull and pleasure crafts); miscellaneous accident (including personal accident); motor; and liabilities.

Source: FSC

The claims experience of the past five years demonstrates the large volatility of losses. In fire insurance, the gross claims ratio fluctuates around 30 percent of gross premiums. However, in 1999 as a result of the protracted drought it jumped to 242 percent. Yet, because of the use of nonproportional reinsurance treaties, the net claims ratio did not exceed 100 percent of net premiums. Fluctuations in the net claims ratio are thus much smaller than in gross claims.

Like long-term business, general insurance also exhibits sound financial ratios (Table 9). Net claims ratios are low by international standards. Acquisition costs benefit from the high commissions received from reinsurers. These exceed the commissions paid to local agents and thus cover some of the overhead expenses of local companies. As a result, net administration and acquisition costs amount to about 15 percent of gross premiums, although they represent 30 percent of net earned premiums. Investment income amounts to 25 percent of net earned premiums. As already noted, the profitability of general insurance business is affected by the volatility of claims and the need to build adequate reserves

Table 9: Financial Ratios of General Insurance, 1997-2001

(percent)	1997	1998	1999	2000	2001*
Ceded Premiums/Gross Premiums	48.8	47.0	48.0	49.1	47.3
NEP/Gross Premiums	50.2	53.4	52.7	49.3	51.3
Net Claims/Net Premiums	55.8	62.9	74.6	65.7	62.5
NIC/NEP	59.2	69.2	74.1	73.3	68.9
Net Commissions/NEP	-3.8	-4.4	-5.2	-6.5	-5.4
Admin Costs/NEP	29.6	31.0	32.4	34.5	35.1
Combined Ratio/NEP	84.9	95.8	101.4	101.2	98.6
Underwriting Result/NEP	15.1	4.2	-1.4	-1.2	1.4
Investment Income/NEP	21.1	23.8	26.0	25.8	25.8
Profit/NEP	36.1	28.0	24.6	24.6	27.2

NEP: Net Earned Premiums; NIC: Net Incurred Claims

* excluding Secura

Source: Estimated on the basis of data collected by the FSC.

Measuring the profitability and solvency of different classes of general insurance business depends not only on their claims and expense ratios but also on the adequacy and appropriateness of their reserving policies. General insurance companies in Mauritius are required to establish reserves for unearned premiums, for outstanding claims, and for claims incurred but not reported (IBNR).

On the whole, reserve levels seem both adequate and appropriate (Table 10). The unearned premium reserve ranged between 48 and 53 percent of net earned premiums, while the reserve for outstanding claims fluctuated between 94 and 110 percent of net incurred claims. This implied that claims were settled with an average delay of one year during this period.

However, the adequacy and appropriateness of reserve levels cannot be ascertained without direct knowledge of the business of each insurer. A low level of reserves, especially for outstanding claims, may reflect short delays in settling claims or it may be caused by inadequate reserving in the face of protracted disputes. Similarly, a high level of reserves may reflect conservative reserving in the face of such delays or it may be caused by excessive reserving in order to understate profits and lower tax liability.

Table 10: Reserve Levels of General Insurance, 1997-2001

(percent)	1997	1998	1999	2000	2001*
Unearned Premium Reserve/NEP	53.0	49.5	49.1	51.4	47.8
Outstanding Claims Res/NIC	109.6	98.7	94.2	100.7	99.0
Total Reserves/NEP	117.8	117.8	118.8	125.2	116.0

NEP: Net Earned Premiums; NIC: Net Incurred Claims

* excluding Secura

Source: Estimated on the basis of data collected by the FSC.

Reserve levels in Mauritius vary considerably across companies and across classes of business as well as over time, even within the same companies. In the absence of either a rigorous inspection program or a requirement on companies to employ experienced and qualified auditors and actuaries for ascertaining reserve levels, it is not possible to judge their adequacy and appropriateness.

As in long-term insurance, there is considerable variation in the performance of general insurance companies by size (Table 11). Small companies are preponderantly involved in motor insurance where they generate 76 percent of their premium income against 34 percent for large companies.

Table 11: Performance and Company Size of General Insurance, 2001

(percent)	4 Large Companies	7 Medium Companies	6 Small Companies*	All Companies
Total Premiums	56.1	35.1	6.9	100.0
Total Motor Premiums	43.0	41.4	11.9	100.0
Motor Prem/Gross Premiums	34.2	52.6	76.0	44.5
Reinsurance/Gross Premiums	53.9	38.2	36.8	46.8
Gross Claims/Gross Premiums	49.9	53.1	66.5	53.1
NIC/NEP	67.9	71.1	64.2	68.9
Net Comm/NEP	-9.6	-1.1	-1.3	-5.4
Admin Costs/NEP	28.7	41.5	40.5	35.1
Net Costs/NEP	19.1	40.4	39.2	29.7
Combined Ratio/NEP	87.0	111.5	103.4	98.6
Underwriting Result/NEP	13.0	-11.5	-3.4	1.4
Invest. Income/NEP	20.7	29.3	37.7	25.8
Profit/NEP	33.7	17.8	34.4	27.2

NEP: Net Earned Premiums; NIC: Net Incurred Claims

* excluding Secura

Source: Estimated on the basis of data collected by the FSC.

Small companies also report a lower reinsurance ratio than large companies (37 against 54 percent). However, the aggregate data conceal the fact that, because of their smaller capital and risk retention capacity, small companies tend to rely more on reinsurance in each class of business. This is hidden in the reported overall reinsurance ratios because motor insurance, in which small companies specialize more, is a line that relies less on reinsurance.

Large companies receive much more on commissions from their reinsurers than what they pay out to their agents. Their administration costs are also much lower than for medium and small companies. As a result, their net costs absorb 19 percent of net earned premiums against 40 in the case of medium and small companies.

Large companies report a significant positive underwriting result in 2001 against losses suffered by medium and small companies. This was partly or fully offset by higher investment returns earned by medium and small companies respectively. The overall profit margin is quite healthy, although no firm conclusions can be derived without more precise knowledge of the adequacy and appropriateness of reserving policies.

VI. Motor Insurance

Motor insurance is the largest class of general insurance, accounting for 45 percent of total nonlife premiums in 2001. It represents the main long tail class of business, but generally reports low levels of claims ratios, particularly by the standards of most developing countries.

Motor claims, especially those that involve only material damage, tend to be settled quickly. However, claims arising from accidents involving bodily injuries are sometimes protracted by disputes between some small companies and claimants.

Motor insurance, even the compulsory part, is not subject to premium control. However, bodily injury liability is unlimited and this creates problems with reinsurers who press for a cap on liability.

The market for motor insurance is much less concentrated than that for other classes of business. The largest 4 companies accounted for 43 percent of total motor premiums in 2001, while the smallest 7 had 15 percent of premiums. The latter compared with less than 6 percent in each of the other classes. The Herfindahl index amounted to 866 in 2001. Not surprisingly, small companies had 22 percent of the number of motor policies in force.

As in most other countries, and despite the absence of tariff controls and prevalence of low loss ratios, motor insurance faces some pressing policy issues. At one level, there are the problems created by the companies that have been put in liquidation and the need for the creation of a viable compensation fund. Then, there is a need to establish an insurance information bureau to collect market-wide statistics on underwriting practices, loss experience, and incidents of fraudulent claims.

A further issue concerns the introduction of a system that would allow statements of fact to be jointly completed by all parties to an accident and filed with their respective insurers for processing (“constat a l’amiable”), doing away with the need for police presence. This will lower the administrative burden of motor accident on the police but some small insurers express concern about the shift of the administrative burden to them. They also fear that less sophisticated drivers could be intimidated by more aggressive drivers.

Another point of contention is the high registration fee of 11 percent on the value of cars that is assessed every time there is a change of ownership. It is argued that to avoid the registration fee ownership changes go unreported and cars are insured in the names of previous owners. Small insurers are also afraid that the proposal to eliminate the requirement for a road license for motorcycles may encourage some motorcyclists to drive uninsured.

The absence of any provisions to cover uninsured as well as bad drivers probably explains the presence of small companies that specialize in motor insurance. Organizing a bad risk pool, like the setting up of a compensation fund, faces difficult problems of its own, but relying on under-capitalized and under-reserved companies to serve this market does not seem to solve the problem. Most of these issues are inter-related and require a global approach after detailed consideration of available options and extensive consultation with all parties concerned.

VII. Regulation and Supervision

Insurance regulation and supervision is entrusted to the Financial Services Commission (FSC). Since its creation, the FSC has taken steps to improve the regulatory framework and strengthen supervision. The current regulatory framework contains many positive features. These include the absence of tariff and product controls, the reliance on solvency monitoring, the extensive use of international reinsurance facilities and the use of international accounting standards and internationally acceptable actuarial methods.

However, there are also some important shortcomings. Solvency margins deviate from prevailing international practice, while regulations on corporate governance, internal controls and risk management need to be brought in line with emerging international norms. Moreover, no “whistle blowing” responsibilities are imposed on actuaries and auditors.⁸

A minimum capital of MUR 25 million is required for setting up an insurance company. The proposed new rule that will impose the creation of separate companies for long-term and general insurance business will effectively double the minimum capital requirement. However, given the large number of insurance companies, a further increase in the minimum capital may be advisable.

⁸ The importance of these aspects of the regulatory and supervisory framework are stressed in Savage (1998) and Thompson (2001).

There is at present no risk-based capital requirement. For general insurance, the required solvency margin is related to annual premium income and is equal to 20 percent of net premiums up to MUR. 30 million, falling to 10 percent for higher volumes. No minimum retention ratio is used in calculating the solvency margin. Despite the risk of encouraging the practice of “fronting”, whereby local insurance companies act effectively as brokers of foreign reinsurers, the lack of a minimum retention ratio in calculating the solvency margin is consistent with the high volatility of insurance claims and losses in Mauritius and the limited local capacity to retain large risks.

There is no solvency margin that is set in relation to claims, a provision that is used in the European Union and has been widely adopted around the world. A claims-based solvency margin prevents companies that charge unreasonably low premiums from operating with low levels of capital in relation to their claims.

For long-term business, the amount of admitted liabilities must not exceed the amount of the long-term insurance fund, but there is no requirement for the maintenance of a positive solvency margin or for risk-based capital.

Admitted assets exclude loans and claims on related parties (directors, agents and affiliated companies), premiums receivable that are outstanding for more than 12 months, intangible assets, and assets held outside Mauritius, including claims on reinsurers that are outstanding for more than 6 months. Housing loans secured by a mortgage in favor of the insurer are included in the definition of admitted assets.

A prescribed investment ratio is applied whereby 30 percent of admitted assets must be invested in prescribed assets. However, the latter are defined very broadly and include government bonds, corporate securities, unit trusts, or bank deposits. The only exception is the exclusion of housing loans and mortgages. Given that housing loans do not suffer from high delinquency rates, they would seem ideal for matching the long-term liabilities of life insurance and thus for inclusion in any minimum prescribed ratio. The rationale of having a minimum prescribed ratio of such broad scope needs to be reconsidered with a view to eliminating it. Reliance on the “prudent expert” principle would be more in line with best international practice.

The most binding restrictions on investments are the limits on overseas assets. Insurers carrying on general insurance business are not allowed to invest in overseas assets any part of their technical reserves and share capital. Mauritian companies engaging in long-term business may invest up to 25 percent of the long term insurance fund in overseas assets. However, foreign companies engaging in long-term business suffer from unfair discrimination since they are subject to a 100 percent localization requirement and are not allowed to diversify their assets by investing overseas.

The setting of technical reserves is subject to a general requirement whereby all insurance reserves and provisions must be calculated in accordance with internationally approved methods. The methods used, and any changes in them, must be disclosed to the FSC, . Most companies maintain strong reserves and provisions, even though the regulator is not authorized to vet the assumptions used by actuaries regarding loss

experience, interest rates, and mortality, nor to control the amount of credit taken for amounts recoverable from reinsurers. Only long-term business requires an actuarial valuation of liabilities. However, the regulatory authority has considerable power to influence actuarial calculations since it may revoke a license if it is not satisfied that an insurance company operates in accordance with sound insurance principles.

Reinsurance arrangements are reviewed by the regulatory authority, which has the right to require any changes that it deems necessary. There is a requirement for compulsory cession of 5 percent of premiums risks to the Statutory Reinsurer, which is Africa Re, but otherwise companies are free to make their own reinsurance arrangements.

One problem is the absence of a strong and effective supervision, although considerable progress has been made over the past couple of years. Filings of audited accounts and financial statements must be made eight months after the end of each company's financial year. Submission of extensive statistical forms is required, but improperly completed forms are often filed by some companies and no corrections seem to be demanded.

Prior to 2001, no on-site inspections had been conducted for almost a decade. The audited accounts of one company showed that it had accumulated large losses that exceeded its paid-up capital and was thus operating with negative equity. Despite a qualified report by the auditor, no action had been taken. Another company had outstanding loans to directors that exceeded its net worth. (Both of these companies took corrective action in 2002.)

Insurance supervision has been invigorated since April 2001 and especially following the creation of the FSC. On-site inspections have been resumed. Three weak companies were put on the "watch" list in 2002. One is now under administration and will probably be liquidated, joining another company that was intervened in 2000. A second company has been restructured with an injection of new capital from a Sri Lankan company. The third company has reportedly been able to strengthen its financial condition and will probably be removed from the watch list.

VIII. Future Prospects and Policy Issues

The future growth of the insurance industry depends on continuing macroeconomic stability, sound regulation and avoidance of company failures and scandals that would mar the good reputation of the industry. The leading companies have a strong record of innovation and efficiency and have been responsive to the changing needs of their customers. The main challenge lies in strengthening the effectiveness of supervision and modernizing the legal and regulatory framework. A consolidation of the industry by encouraging weak firms to merge or exit the market would also contribute to sounder competition and greater safety.

Two new draft insurance bills are under consideration. These aim to modernize the legal framework and address most of the current gaps in regulation and supervision. They introduce new rules on corporate governance and the responsibilities of directors,

on internal control and risk management systems, and on the duties of actuaries and auditors. They also require the creation of separate subsidiaries for engaging in long-term and general insurance.

As part of the new framework, detailed standards should be issued covering the constitution and methods of calculation of reserves and provisions and the amount of credit for amounts recoverable under reinsurance arrangements to ensure that all companies follow sound policies. While accounting and actuarial practices used by most companies are in line with best international practice, the FSC should be able to challenge all assumptions used by actuaries in the valuation of technical provisions, especially in the case of smaller companies.

Capital adequacy standards should be brought in line with best international practice. The EU standards on solvency margins are widely used and are not hard to administer. A solvency margin based on average net claims over a specified period (between 3 and 7 years depending on the volatility of losses) should be introduced to complement the solvency margin that is based on net premiums. A positive solvency margin requirement for long-term business should also be applied. The application of EU-type solvency standards could be seen as a transitional step toward the introduction of risk-based capital requirements, i.e. requirements that take into account the volatility in the market values of assets and liabilities.

Consolidation of the insurance industry needs to be promoted to ensure sounder competition and greater safety. This can be achieved by raising the level of minimum capital and introducing risk-based capital requirements as well as by encouraging weak firms to merge with other firms or exit the market. The need to cover the high-risk segments of the motor insurance market could be addressed more effectively by supporting the creation of a national pooling arrangement by the Insurers Association.

An insurance information bureau should be created with data on underwriting policies, loss claims and incidents of insurance fraud. The bureau should facilitate sharing of these data by all licensed companies and should contribute toward higher underwriting standards. Competition policy should ban the practice of tied sales whereby customers of large companies are forced to buy several services from the same group. These practices discriminate against smaller firms.

Consideration needs to be given to the creation of a compensation fund to cover the unpaid claims of failing companies and protect policyholders, especially in connection with life and annuity policies. Special provisions would be required to expedite the liquidation process, require the submission of reorganization plans, and facilitate the reinsurance and/or transfer of policies. These measures would protect the assets of the failed companies from the expenses of protracted liquidation and thus maximize the amounts available for distribution to policyholders and other claimants. However, as in the case of deposit insurance schemes for banks, effective supervision and risk-based capital requirements would provide a better safeguard against such losses.

Although the likelihood of a large and persistent fall in the level of interest rates seems remote at this juncture, the FSC would be well advised to require company actuaries to report on the sensitivity of company balance sheets to such an event. The undertaking of dynamic solvency tests would be motivated by the current duration mismatch of assets and liabilities that is caused by the dearth of long-term assets in the local financial system on the one hand and the prevalence of endowment insurance policies and group pension business on the other.

Regular reporting of the exposure of insurance companies to reinvestment risk would encourage early action to avoid the recent experience of several European countries. It would also reinforce the case for the issuance by the government of long-term bonds (inflation-linked, zero-coupon or other) that would provide a better match to the liabilities of insurance companies.

To strengthen the effectiveness of supervision, the FSC has plans to develop a sophisticated early warning system that would enhance the quality of off-site surveillance and would help identify companies in difficulty. On-site inspections would need to be better organized, to be focused on weak companies and to emphasize the importance of good corporate governance and adequate internal controls and risk management systems. The adequacy and soundness of reinsurance arrangements should to be regularly reviewed.

There is considerable need for hiring experienced and high caliber professionals and for training to upgrade supervisory skills. Increasing contact and cooperation with actuaries and auditors would help alleviate the workload of insurance supervisors and would address the current skills deficit.

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