CHAPTER ONE

1.0 INTRODUCTION

1.1: BACKGROUND

The business of banking and insurance has gone through massive transformation the world over and Nigeria is not an exception. These transformations, though not without their "draw backs", have definitely added some quality to the services rendered by banking and insurance industries at large. ***Ezeduji: (2000: 8)***

One of the major disadvantages of specialization is that it results in monotony. The Oxford Advanced Learner's Dictionary defines monotony as "boring, lack of variety". It then follows that specialization made it possible for banks and insurance companies to be classified according to the services they offer. Commercial banks were restricted to "Retail Banking", merchant banks were statutorily required to engage in "Wholesale Banking". Insurance companies were registered primarily as risk bearers but must operate as "Life Only Company", "General Business Only Company", "Composite Business Company" or "Reinsurance Company".

That specialization brought about efficiency in the Nigerian financial system is a true statement but as time went on, the needs of people went beyond the scope of specialization, and the needs for banks and insurance companies to widen their range of service became necessary to meet the customers' demands. This research work highlights the challenges of the insurance industry under the Universal Banking Scheme in Nigeria.

1.2: UNIVERSAL BANKING IN NIGERIA - INTRODUCTION

The early confusion that heralded the concept of Universal Banking (UB) appears to be over more so after the publication and circulation of the Draft Guidelines on Universal Banking in August 2000 by the Central Bank of Nigeria (CBN).

Universal Banking is a system in which banks are free to choose which activities they wish to undertake (money or capital market activities or insurance marketing activities or a combination) and are expected to comply with the guidelines specified for such activities, in which case there will be no restrictive cause.

The greatest impetus in adopting Universal Banking (U.B.) in Nigeria has been attributed to the changes in her laws and regulations. These changes in laws and regulations were responses to the pressures mounted by banking institutions to be allowed to expand the scope of their activities.

In Nigeria, there is evidence that the distress and failure of many banking houses, as well as diminishing profitability of others brought about the clamour for universal banking practice in the country to create a level playing field. Prior to the adoption, in principle, of the concept of U.B. in 2000, in the country, the merchant bank operators were complaining stridently that the playing field was skewed in favor of the commercial banks. ***Chizea (2000: 18)***. He also opined that not only were the commercial banks allowed to participate in what was thought to be the exclusive reserve for the merchant banks such as leasing and related fee-based services, commercial banks, in addition, enjoyed the advantage of having wide scope activities.

The disadvantaged position of the merchant banks, vis-a-viz that of the commercial banks was particularly compounded due to the paucity of long-term funds that would enable merchant banks to

discharge creditably their statutory assigned role of medium and long-term credit creation. These imbalances resulted in relatively reduced level of profitability against the background of rising shareholders' expectations.

To some extent, globalization has contributed to the popularity of U.B. even in economies that do not use the term – Universal Banking, but practice it through partial or complete removal of the differences among the various banks, which hitherto specialized in narrow range banking services. Globalization has contributed to the development of U.B. by motivating the use of information and computer technology, which has integrated the world economy and made each economy to imitate the best practices elsewhere.

The contribution of economic exigencies, market dynamics and trends in international market had led to the reappraisal and re-examination of the structure, scope and functions of banking institutions in the country. The salient feature of U.B is that it removes the restrictions between commercial, merchant banking and insurance marketing, such that a banking institution can offer integrated financial services in a one-stop financial center. ***Imala (2000:27)***

Universal Banking, therefore involves the provision of a range of financial services comprising deposit taking, lending, trading in financial instruments and foreign exchange including derivatives, underwriting of new debts, equity issues, brokerage, investment management and insurance. From a broad perspective, U.B permits financial and commercial linkages such that banks can now own commercial concerns.

1.3: INSURANCE DEVELOPMENT IN NIGERIA-A BRIEF SURVEY

Insurance business was brought to the African continent by the British traders in about 1850. West Africa was purely a trading area and the British government was not directly involved in any part of it.

The export of palm oil, **cocoa** and cotton had become important at that time after the slave trade.

The first attempt at governing Nigeria took place in 1861, with the annexation of Lagos. The big trading company – the United African Company – which is the forerunner of the Niger Company was formed in 1879 together with Elder Dempster of Liverpool, dominated the West African trade and constituted the first British Government administrative framework. Due to their increasing interest in Nigerian trading activities and investments, they got the British Government to lay claim to those areas of West Africa, including Nigeria that came under their protection in 1884.

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They brought shipping, banking and insurance to Nigeria, which contributed to the faster development of the Civil Service, Education and Business in British West Africa. In 1919, the African and Eastern Trade Cooperation, which w as really an amalgamation of the African Association, Miller Brothers and other West African firms, introduced the Royal Exchange Assurance Agency in Lagos.

This was the first Insurance agency in West Africa. It became a branch office the following year.

Egerue (2000:16) maintained that prior to the incorporation of the first set of indigenous insurance companies; offices that were primarily branch offices of the European Insurance Companies with their headquarters based in Europe had underwritten insurance business in the country.

With independence and consequent involvement of Nigerians in all aspects of the nation's economic life, there emerged a few indigenous insurance companies. From 1960 to 1985, a large number of indigenous insurance companies commenced operations, underwriting various classes of insurance businesses and on an aggregate, accounted for about 49.66% of the insurance business in the country. However with the introduction of the Structural Adjustment program (S.A.P) and the increased drive towards indigenous participation in the management and control of business in the economy, a number of insurance companies with government and foreign interest were privatized and commercialized in 1988 thereby enlarging the size of the indigenous insurance that then accounted for about 89.2% of the total insurance business in the country. The leading composite insurance company in the country then was National Insurance Corporation of Nigeria (N.I.C.O.N), which although was faced with imminent privatization, was wholly owned by the Federal Government of Nigeria. It underwrote at least 38% (1987) of the total insurance business in the country.The Nigerian insurance market is the largest in Black Africa and among the leading markets in the third world developing economies. For example in 1967, the total premium income for the total insurance companies in Nigeria was about N18 million. By 1971, it had risen to N37 million and in 1972, to about N55 million. The Gross Premium Income (GPI) further grew from N123 million in 1975 to N608 million in 1984, which represented about 24% of the total G.P.I. written in Africa in 1976. The 1985 figure of N604.4 million showed a marginal increase of 0.4% over 1984 figures, while the 1986 figures rose by 17.2% of the 1985 figures N774.4 million.

The 1987 figures were much substantial an increase of over 49.5% or N1.069 Billion. From the prevailing growth trend the gross premium income for 1988 was N1.4 Billion.

With well over 140 insurance companies, 450 insurance brokers, 30 loss adjusters and over 3000 agents operating in the markets, the insurance industry would not have asked for more. ***Okonkwo. (2002)***

1.4: STATEMENT OF PROBLEM

The major challenges of globalization remain the setting of high standards, which serious business concerns aspire to meet. Meeting those world standards by insurance companies operating in developing economies, such as Nigeria, imposes numerous challenges on such companies and industries especially in the face of the inherent constraints in their respective environments. Universal Banking encourages business operators with adequate capitalization, which would fund profitable diversification into related areas that would add values to customers and improve profitability.

In the light of the above conditions, insurance companies operating under the Universal Banking Scheme would be confronted with so many problems, which solutions were

proffered in the literature review and recommendations. Prior to the adoption of Universal Banking, Insurance Companies in Nigeria were confronted with so many problems namely: -

(a) UNDER-CAPITALIZATION

The level of capitalization of the Nigerian Insurance companies was too low prior to the emergence of the Universal Banking Scheme in Nigeria. The average capital base of an insurance company in Nigeria then was less than N1 Million (one million Naira) while the capital requirement of a Universal Bank was N10 Million (ten million Naira) as postulated by ***Corhen (2000:12)***. Capitalization base problem is a constraint in acquiring the relevant technology and infrastructure needs of an insurance company under the Universal Banking System in Nigeria. Insurance companies have

recently increased their capital base (depending on the class of business the given company is registered to transact) by virtue of the provisions of the Insurance Decree of 1997 but it is yet a far cry from that of the Universal Bank. Returns on investment in the insurance sector were low and slow (given the nature of insurance business), thus creating a kind of apathy by investors who would want to invest. Insurance companies as at now are yet to be adequately capitalized notwithstanding the recent increase to cope with the challenges posed to them by the U.B. scheme in Nigeria

(b) INADEQUATE MANPOWER.

The dearth of manpower requirement and professionalism could impede the smooth and competitive operations of the insurance companies operating under the U.B. scheme in Nigeria. The challenges of inadequate and inappropriate human capital remain pervasive and will always manifest. This is further compounded by the movement of the few qualified insurance professionals to the Universal Banks that have better service conditions, given their superior capital base.

(c) **UNHEALTHY RIVALRY**

There is always the fear that the adoption of Universal Banking Scheme would lead to unhealthy competition and creation of financial conglomeration. Incidentally, insurance companies are not even fair to themselves as some of them sharp-practice while others engage in rate-cutting outside the provisions of the agreed general premium tariff. There are also the problems of merger, augmentation of capital (in the face of the saturated capital market) or more co-operations by pooling the resources of small companies together.

(d) **IMAGE PROBLEM**

Insurance companies in Nigeria are already saddled with image problem. The average Nigerian perception of insurance company is that of a fraudulent institution that will never pay claims to anybody unless after a legal battle. The general low level of the understanding of the insurance technicalities and practices by the insuring public further compounded the problem. ***Nigeria Insurance Annual (1988: 19)***

(e) **HIRACHYCAL CONFLICT/CRISIS.**

There is the feeling that there would be conflict in the tripartite relations between the Central Bank of Nigeria (CBN), Securities Exchange Commission (SEC) and the National Insurance Commission (NAICOM) as to who would subordinate in regulatory matters. It certainly would be an under-statement to think that there would be no conflict. ***Imala, (2000:27)***

1.5: OBJECTIVES

With very strong capital and asset base, backed by adequate re-insurance covers, the introduction of modern technology, the insurance companies will improve their internal affluence and provide better services to their customers under a Universal Banking System. The Challenges of the Insurance Industry under the Universal Banking System in Nigeria became manifest by the empowering of the Universal Banks to widen their scope of operations to include insurance marketing, underwriting and services, more so from an advantageous position of having very superior capital base. The idea of Universal Banking came from the needs to provide the customers with effective financial services under a convenient circumstance and competitive environment. The main objectives of the study are as follows: -

1. To see if insurance companies have adequate capital base to meet the needs of their customers.

2 To assess the impact of human resource adequacy requirement of insurance companies in line with the demands of the Universal Banking system and globalization.

3 To identify the foreseeable challenges the insurance companies might face under the Universal Banking System in Nigeria.

4 To find out if the UB system significantly affects the revenue income of the insurance industry.

RESEARCH QUESTIONS.

(a) Are insurance companies adequately capitalized to operate under The Universal Banking System in Nigeria?

(b) Do the insurance operators have the requisite human resource adequacy to have a good share of the market under the Universal Banking system in Nigeria?

(c) What are the likely problems an insurance company will face under Universal Banking System?

(d) If you were not an employee of an insurance company, given the superior capital base of the banks, where would you prefer to insure your properties- insurance companies or banks?

(e) If you had opportunities, would you prefer to work in an insurance company or a bank?

(f) Are the insurance companies doing enough in creating insurance awareness in Nigeria?

(g) What challenges does the Universal Banking system pose to the insurance industry in Nigeria?

(h) Does the Universal Banking system in Nigeria improve the revenue income of the insurance industry in Nigeria?

1.7: HYPOTHESES

Following the problem statements and objectives of the study, the following research hypotheses were formulated to test various aspects of the basic contention that the Universal Banking practice has reduced the revenue income of the insurance industry.

H_0 1 Universal Banking system in Nigeria does not affect the revenue income of the insurance industry.

H_0 2 Universal Banking system in Nigeria does not pose any challenges to the insurance industry in Nigeria.

H_0 3 Insurance companies are adequately capitalized to operate profitably under the Universal Banking system in Nigeria.

In section 3:9, alternative hypothesis will be provided to ascertain the validity of the above hypotheses.

1.8: SIGNIFICANCE.

The Universal Banking concept is accepted in theory to be of great importance to the economy. It is believed that Universal Banking and Insurance will promote efficiency through the economy of scale, creation of competitive environment, improved customer service delivery and fastening of economic growth through the supply of secured long term finances for commerce and delivery. It also provides a forum for financial conglomeration. The above enumerated aims surely would be achieved in line with the recommendations.

In addition to the overall importance of the study to the economy, the study is beneficial to the following people or groups.

1 Institutional Regulators.

Insurance and Universal Banking will obviously bring about the expected transparency and responsibilities in the financial institutions' system especially the regulators.

2 Insurance companies

The study will unveil the insurance companies' deficiencies as business outfits with a view to improving on them. Through the study the insurance companies would know what are required to operate a profitable insurance business in terms of capital requirements, proficiency, professionalism and institutional regulations involved. The study will also reveal the technological requirements for an insurance company wishing to get a good share of the insurance market under a Universal Banking Scheme.

3 **Research Scholars**

The Study is beneficial to scholars because it will serve as a reference guide to further research on the subject.

1.9 SCOPE AND LIMITATIONS

1.9.1 SCOPE OF STUDY

Scope of study refers to research boundary. The focus is on the challenges faced by the insurance industry under the Universal Banking System in Nigeria. Emphasis is placed on knowing the rudiments, including the institutional arrangements with which the Universal Banking was introduced in Nigeria. It also requires the identification of the rules governing banking and insurance business under the Universal Banking system in Nigeria. Highlights on the performance of non bank-owned insurance companies and those of bank-owned insurance companies, under the Universal Banking system, are imperative. The researcher visited The Universal Insurance Plc, I.G.I. Plc, N.I.C.O.N. Insurance Plc., and Alpha Insurance Brokers Ltd. (all non bank-owned) and Zenith General Insurance Plc., Union Assurance Plc., ADIC Plc. and FBN Insurance Brokers Ltd., all in Enugu for gathering of primary data.

1.9.2 LIMITATIONS

Hardly would a research be conducted without some constraints in Africa and more so in Nigeria. In a country such as ours (Nigeria) where beaurocracy acts as constraints in the flow of information and where there are limited data and statistics, there really have to be problems.

DIFFICULTY IN OBTAINING DATA

Data have been gathered on Universal Banking System in Nigeria but it has not been practiced long enough in this country Nigeria.

To get the exact impact the Universal Banking has on the Insurance Industry, further extensive and long-term data, need to be gathered.

FINANCIAL CONSTRAINTS

A research work of this kind is certainly not free from costs. Given the tough economic situation in Nigeria (high cost of fuel and attendant high transportation costs) the researcher had problems sourcing adequate funds for his movements in the course of this research work.

PRIVACY OF INFORMATION

Some of the senior and management members of staff I approached for information refused on the ground that they lacked the authority to part with such information.

The above constraints notwithstanding, the researcher made very spirited efforts at collecting reliable data. This is to ensure that the research findings have a good degree of validity and reliability.

1.10: DEFINITION/EXPLANATION OF TERMS

Insurance – Insurance is a “Risk Transfer Mechanism” involving two contractual parties namely the Insured and the Insurer. The mechanism provides that the prospective policy holder insures his property or life with an insurance company by transferring from his own shoulders the financial burden of some potential misfortune to the broader shoulders of the insurer, who in return for agreeing to assume a potential risk of loss, receives a payment (from the insured) known as premium. The insurer then promises to indemnify the insured if the insured event occurs. The insurer, by collecting sufficient amount of premiums, relies on the probability that only some of the risks/losses he insured against would actually occur within any given insurance period. The insurer therefore calculates that he would be left with a profit. The insured, having freed himself by means of insurance from certain types of worries, is better enabled to risk his capital in trade, since he knows he cannot control certain fortuitous events like fire, shipwreck, e.t.c. ***Hansell, D.S (1985:22)***

Life Only Company – This is a duly incorporated and registered insurance company in line with the provisions of Companies and Allied Matters Act of 1990 and authorized by the National Insurance Commission to transact only Life Business.

Re-insurance – Re-insurance is a contract whereby the insurer (otherwise known as the Direct Insurer, ceding company or the re-insured) retains certain percentage of the risks he insures in line with his retention capacity and insures the surplus with another company, usually called the Re-insurer.

Gross Premium Income – This is the total amount of premiums collected by an insurance company in respect of all the classes of insurance written in an insurance year.

Indemnity – The law provides that the insurance of property and liability should be subjected to the principle of "Indemnity", so that the insured will be unable to receive an amount more than his financial loss, which results from the event that was insured against. Insurance may be for less than a complete indemnity, but as a rule, it must not be for more. It is not desired that an insured will make a profit out of an insured, fortuitous event. If that is the case, then, there will be more fire, burglary, accident and marine claims, hence the provision for the principle of indemnity. ***Nwafor, (2005:81)***

Banking – Banking is the business of receiving money from outside sources such as deposits, irrespective of the payment of interest and the granting of loans and acceptance of credits or the purchase of bills and cheques or the purchase of sales of securities

for the account of others or the incurring of the obligation to acquire claims in respect of loans prior to their maturity or the assumption of guarantees and other warranties for others or the effecting of transfers and clearing and such other transactions as the Minister may on the recommendation of the Central Bank of Nigeria, by ordering its publication in the Federal Gazette, be designated as banking service. ***Uremadu (2000:30)***