A Study on the Corporate Demand for Insurance

This report investigates the various types of risks a firm is exposed to and the corporate expenditures and incentives for the purchase of insurance policies to hedge those risks. Specifically, in Chapter 2, We examine the corporate expenditures on insurance products in Korea by industry and by firm size using Use Tables, Input-Output Tables and Financial Statement Analyses. The aggregate corporate spending on insurance had increased at an average annual rate of 7.7% since 2011 and reached to 14.23 trillion won in 2017 which accounts for 0.82% of the GDP. The average insurance premium-to-sales ratio also increased from 0.28% in 2011 to 0.36% in 2017. According to the Financial Statement Analysis, while the manufacturing industry accounts for 47.5% of the entire corporate sales and 34.2% of the insurance premium, the premium-to-sales ratio of the manufacturing industry is only 0.26%. During the period from 2011 to 2016, the insurance premium paid by the small and the medium-sized firms grew at a much faster rate than that of the large and established firms (10.7% vs 2.3% per year). As a result, the small and the medium-sized firms occupy 70% of the total insurance spending in 2017. Similarly, the average premium-to-sales ratio of the small and medium-sized firms is 0.6%, which is three times greater than 0.19% of the large firms.

In Chapter 3, we review the existing literature on incentives for the purchase of insurance policies by firms. Based on that, we investigate the impact of expected bankruptcy costs, a convex tax function, investment incentives, and macroeconomic factors on corporate spending on insurance, using the data set consisting of 168,989 firm-year observations during the period 1999~2017. We find that the firm level factors and macroeconomic conditions, such as GDP

growth rate and the won-dollar variability, have economically and statistically significant effects on the demand for insurance.

Chapter 4 presents the results of the risk perceptions and management survey conducted on 824 firms in 2019 in Q2. The survey highlights the shift of risk toward non-physical damage events beyond the physical perils like fire and natural catastrophes, and the growing inter-connectivity of risk faced by firms. Supply chain failure, which is ranked as fifth risk, is increasingly being caused by non-traditional risk exposures such as geopolitical uncertainties and cyber issues. Business interruption, which is ranked sixth, is influenced by several of the top five risks including supply chain failure and physical perils. Most perils related to supply chain failure and business interruption today are not covered by traditional insurance products. As the gap between economic and insured losses continues to widen, the demand for insurance products changes. A range of new risks is emerging, beyond the perils of fire and natural catastrophes, and which require rethinking of current insurance coverage.