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Risk Management, Corporate Governance and Performance of Insurance Companies in Nigeria

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ABSTRACT

The purpose of this paper is to examine the impact of risk management on organizational performance of insurance companies in Nigeria. The study considers multi-sampling techniques since the population of insurance companies in Nigeria is fifty-nine (59) and all the population could not be covered, so Sixty percent of the population was covered which amount to thirty-six (36) insurance companies. The study revealed that risk management, strategic decisions and corporate governance indicate a significant relationship with organizational performance by showing a positive relationship. Effective management of risks by insurers will increase the performance and profitability of insurance companies in Nigeria. Risk management is a crucial issue, not only for the survival and profitability of the insurance industry, but also for the economic growth and development of the whole economy. As major risk underwriters, insurance companies need to adopt good and quality measures in the management of operational risk. This is important, more so, as the industry prepares to recapitalized their capital base and reform the sector. Research into impact of risk management on the organizational performance of insurance

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companies from Nigerian perspective is rare. This study is therefore timely and its findings are invaluable for the efficient management of operational risk in the insurance industry.

Keywords: Risk management, organizational performance, corporate governance and strategic decisions.

Jel Codes : Gel 22, Gel 34

Introduction

A goal led competition among individuals and business organizations has resulted into a huge volatility of the market force (Yeshitila et al., 2020). It has undoubtedly brought about a lot of risk incurring and strategically managing these various types of risk recorded becomes a matter of necessity and the responsibility lies with the insurance companies that are encumbered with the responsibility of mitigating risk faced by individual or business organizations. Insurance companies manage third party risk that can be carried out by orderly strategic risk management processes so as not to impair their capital base. Policy holders transfer their risks to insurers in order to mitigate unforeseen events which may cost them the entire property or part of the property and their willingness to pay in return premium as agreed upon in the terms of the insurance contract. Insurance companies undertake risk on behave of their clients by pooling all the risks of policy holders through various products with a promise to indemnify the policy holders in case the unforeseen happened. It should be noted also that insurance industry do contribute enormously towards the growth of economic activities as they do participate actively in the capital markets by investing their surpluses in stocks, bonds and in other capital market instruments for them to earn more income to support their desired need of helping their clients to mitigate against risk as the case may be. In the process of redistributing

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risk across different cohort of insured that takes up insurance policy, insurance companies face different types of risks that might have evolved from their internal and external environment that need to be managed but if not well taken care of could lead to catastrophic loss that will threaten their existence. It is pertinent therefor for the insurance companies to have better understanding on the likely risks that is associated with the various policies for them to know how well to manage these risks and also to be able to survive their competitive environment. It is therefore necessary for managers of the insurance companies to rise to the task of risks management in this dynamic world where it is very difficult to predict the economic situations even at the shortest future period. Strategic risk management is therefore the order of the day if you are out there to meet up with the desires of risk policy holders and the quest of your organization to make profit and survive competition in the industry. Effective corporate governance that is highly stimulus to strategic risk management will help in a long way in the management of this sensitive sector of the economy who has decided to pool various risks of policy holders in order to indemnify any when the projected risk eventually surfaced. This task requires the integration of strategic risk management practices into insurance companies' management, processes and culture so as to make profit and perform better (Kokobe & Gemechu, 2016).

Historically, many corporate failures have been associated with the relegation of risks and this may turn out to be fatal in the future. After the last financial crisis in 2009 and the new Covid-19 pandemic, the significance of strategic risk management and corporate governance became significant issue in the insurance industry and their applications will help the industry to confront the challenges that arose as a result of changes in the economic situation (Richter & Wilson, 2020). Consequently, a clear understanding of business strategies that are associated with risks is necessary as this will help to oversee the managerial

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operations and strategy formulation process of the industry. Strategic risk management is associated with identification, evaluation, coordinating and analysing the risk exposure that arises from an unexpected outcome and the application of available resources to minimize, monitor and control the probability of unfortunate events and realization of opportunities will be highly required to confront the changes in the economic system (Arunga & Njunguna, 2012). Managements are expected to intensify efforts in the formulation of risk management policies and procedures that will help in meeting the demand of the prevailing situations. The objective of this is to analyse the risks borne by individuals, business organizations, banking financial institutions, non-banking financial institutions and public institutions in order to suggest action(s) in order to confront and mitigate against expected risks. Since strategic risk management is a never-ending process that consist of different steps, the policies and procedures put in place for proper strategic risk management practices should be formulated as an ongoing activity in the organization and this should be flexible enough to meet up with any future crisis as the situation arises. Strategic risk management also comes with setting appropriate environment to protect the financial institutions from adverse outcome or risk exposure. This can be achieved through the identification of events into one or more broad categories of market, credit, operational and other risks, assessment of risks using data and risk model, monitoring and reporting of the risk assessments on a timely basis to pacify the effect of the risks by senior management (Ebenezer and Omar, 2016).

Maher and Anderson (1999) viewed corporate governance as the rules and regulations set aside for the investors to follow so as to make return on investment and to make sure the managers of fund did not misuse the investors' funds and create value for the owners of business organizations. There is need for transparency in the governance of corporate organizations which have been

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the concerns of standard setters all over the world. These needs have resulted in a renewed interest, in the corporate governance practices of insurance companies, particularly in relation to objectivity, accountability, profitability and honesty which will bring about performance in the industry (Jayeola & Olufemi, 2011). Corporate governance also demands for stewardship in insurance industry as managers of these companies are expected to act in the best interest of the firm's owner and shareholders most especially, the minority shareholders or investors, by ensuring that only actions that facilitate delivery of optimum returns and other favourable outcomes are taken at all times (Lee, 2003). As a result of this an effective corporate governance structure is expected to promote sound internal control system, effective risk management, compliance with ethical and statutory requirements, ensures transparent and efficient markets, accountability and trust in the management of such organisations (OECD, 2014).

Organizational performance is measured by the best way through which the available scarce resources can be utilized to generate more revenue for the organisation. The performance of the insurance companies is very important towards the growth in the industry and the economy as a whole. This will also determine the overall performance of the clients of the insurance companies. The performance of the insurance companies can be measured in terms of profits and investment using annual turnover, underwriting profitability, return on asset, return on investment, net premium, earned returned on equity, solvency and liquidity. This subjective measurement states how well an organization can use assets from its primary mode of business to generate revenues which determine the financial health of the organization over a given period of time (Ironkwe and Osaat, 2019). For insurance industry to be effective, there is the need to apply strategic risk management for sustainability, survival and financial performance

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of the industry. Behind those profit motive, there is need also for managers to make good strategic decision and also implement good risk management practice into their system. such decision(s) if properly made will assist the organizations to excel and have competitive advantage over their competitors. It shows therefore that an organization makes strategic decisions in order to reach their set goal(s). Each strategy has related/associated risks that needs to be managed appropriately if set goals are to be attained as at when due. The timing of projected cashflows needs to be properly monitored for the organisation to be on track in all ramifications.

The issue of strategic risk management, corporate governance and organizational performance of insurance companies in Nigeria came with unethical related issues. But the rate at which risk management and corporate governance affect performance remain unclear because of the applied theoretical perspective of risk management and the creation of theory of corporate governance on performance of insurance industries in Nigeria. Applying good risk management drives corporations to push ahead and make steep gains.

Extensive research exists on the relationship between Risk management and financial performance of insurance industries in Nigeria. But none of these studies focus on the effect of strategic risk management and corporate governance on organisational performance of insurance companies in Nigeria. The objective of the study is to consider the impact of risk management, strategic decisions and corporate governance on organizational performance of insurance companies in Nigeria.

The paper is divided into five sections - Section one introduces the subject matter, while section two presents a review of literature. Section three describes the research methodology employed for the study, while section four focuses on research findings. The last section which is section five concludes and provides

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recommendations of the study.

Literature Review

There is the need for the insurance companies in Nigeria to rise up to the challenges facing the industry as a result of the world financial and economic crisis. Many countries are already battling with financial crisis before the advent of Corona Virus pandemic (Covid-19) which totally put a hurt on economic activities in most parts of the world. As a result of this, the insurance companies in Nigeria need to upgrade their capital base for them to be able to confront the present challenges in line with the trend in the economic environment. This can best be achieved by employing strategic risk management processes and implementing good corporate governance in order to mitigate the effect of risk in insurance industry (Gurtner, 2010). Wiebe et al, (2008) identify the followings as the primary risks that insurance companies should mitigate against for them to enhance their performances. These include - market risk, credit risk, funding/liquidity risk, operational risk, underwriting risk, reputation risk, financial/reporting reliability risk, legal/regulatory/compliance risk, information technology risk and other risks. One of the most significant remarks is that risk is in derived category and cannot be addressed directly without previous investigation into the objectives, contexts, hazards, vulnerability, resilience and interested parties. It is important to take note of the potential contradictory interpretations of concepts in conducting risk analysis as this will help in the assessment and management of such risks. However, it has been observed that one of the best possible strategies when dealing with risk management is the avoidance of any identified risk by considering different safety measures (Aleksandar & Radenko, 2015).

Risk management can be defined as the process of identifying, analysing,

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assessing, monitoring and controlling risk and adopt better process of strategic decision making in an organisation (Saleem & Abideen, 2011). Any company that implements good strategic risk management practice into their organization are likely to perform better financially and also have competitive advantage over their competitors in the market. Identification of risk is the first and perhaps the most important step in risk management process. It is when risk is identified that we can be talking about the management of such risk. When risk involved in an investment cannot be identified, then it will not be possible to apply other steps in risk management process and thereby mitigating against such risks in the organisation (Ana-Maria & Ghiorghe, 2014). Risk identification is considered to be the most important step in risk management process because it provides the foundation for the right future activities of the organization concerning the development and the implementation of new programs for risk control (Tchankova, 2002). Identification is seen as a team work which looks at project events with respect to various risk categories and extracting those which could have a negative impact on the project. However, it should be noted that the business environment is dynamic, therefore, the process of risk identification must be continuous (Russell, 2018). After the identification of risks, the next step will be to assess the impact of the risk in quantitative terms to ascertain what will be their effect on the performance or output of such organisation if efforts are not put in place to mitigate against such risks. Such assessment will enable the organisation measure the effect of such risk(s) against the cost they will put in place to mitigate against such risk(s) (Ahmed et al, 2007; Olivieri and Pitacco, 2011). At this stage, risks identified are ranked and prioritized. This will help in better understanding of the possible impact of a risk or the likelihood of its occurrence (United Nation, 2012).

The evaluation stage usually depends on the number of risks. However, when

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there are only few risks then the evaluation stage might be lightweight, but, when there are much menace and the situation is complex, then the evaluation becomes difficult. Moreover, in the evaluation stage risk should be examined individually, as well as their combined impact on the output of project (Saleem & Abideen, 2011). Risk evaluation entails the assessment of the level of damage so as to make decisions about further risk treatment. This involves comparing the level of hazard as determined during the risk analysis and risk evaluation. This will help to defined the risk criteria in order to prioritize the implementation of adequate measures for treatment and mitigating of such risk (ISO, 2009). The importance of risk management process is the risk treatment. Risks that are worth of further investigation should be due to either of their relative importance or because of their high chance of reoccurring. Risks can be treated either through proactive approach or through reactive approach. Reactive approach refers to the actions initiated after the eventuation of the risk's events, while proactive approach refers to actions initiated based on chance of the occurrence of certain risks (Ariff, 2014).

It is necessary to ensure that changing circumstances do not alter priorities such as facilitating easy identification and treatment of new risks as they arise. It is therefore, paramount to maintain adequate process records for monitoring and reviewing purposes (Tularam and Attili, 2012). Risks are needed to be monitored regularly, to ensure that changing circumstances do not alter the steps taken against identified risks. Some risks are likely to remain static, nevertheless, risk management process should be performed on regularly bases, in order to capture new risks and effectively managed them (Vasile & Croitoril, 2012). There is need to communicate risk which is seen as an integral part of all risk management activities that take place at all stages of the risk management process. This entails engaging internal and external stakeholders through the risk

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management process. The framework promotes 'consultative team approach' in order to facilitate good communication with key stakeholders from the outset (ISO31000:2009). In future, the face of risk communication will be two folded: First, organizations have to expand their internal communication, secondly, the demands of external stakeholders will likely increase (Lee & McGannon, 2005). Organizations must establish a proper communication strategy to support effective communication and consultation. Moreover, focus should be on consultations which make it important that stakeholders must be communicated throughout the risk management process and after that, their perceptions must be recorded which would be helpful in decision-making.

Chipa and Wamiori (2017) in their study investigated the impact of risk management on insurance company's financial performance. Their findings revealed that independent variables namely liquidity risk management, operational risk management and enterprise risk management have significant influence on financial performance of insurance companies in Kenya.

Ebenezer and Omar (2016) assert that managing risk does not often translate to positive performance. Although effective strategic risk management and applying strategic risk management in financial institutions reduces the occurrence of systemic and economic breakdown, but this does not guarantee an increase in the returns on equity.

Abideen and Saleem (2011) report the current practice of risk management in Pakistani software development sector. The result of the study shows that risk management was not widely practice and most of those organizations documented risk policy. It was established from the study that ineffective documentation and practice of risk management affect companies' performance negatively.

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Owolabi et al (2017) in their study mentioned that every economic activity is faced with both internal and external risks which could deprive profit making motive of companies. Considering the increase in risk in organization, managing risk is a matter of necessity. Business put great emphasis on hazard administration as this determines its survival and business performance.

Kaplan and Mikes (2012) in their study mentioned that selecting a particular risk management tool tends to be associated with the firm's calculative culture and the measurable attitudes that senior decision makers display towards the use of risk management techniques. Furthermore, the poor risk management and laxity on the part of management in the banking and non-banking financial institutions often lead to the deterioration in capital adequacy and have a direct influence on the shareholders' funds.

Kokobe and Gemechu, (2016) in their study shows that risk management practice and financial performance are not correlated. It was opined that it opens a door for other problems on the application of the management techniques. Insurance companies should adopt enterprise risk management that is currently the best standard practice and they should also apply risk management techniques effectively so as to improve on their returns on equity and reduce loss ratios.

Kamau et al (2018) in their study sought to determine the influence of corporate governance and strategic choices on performance of financial institution in Kenya. Cross-section descriptive research was adopted and primary data collected from top executive of 108 financial institutions. It was affirmed from their study that corporate governance and strategic choices influence positively organizations' performance.

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Methodology

The data collection instrument used in gathering the data was a comprehensive modified questionnaire that was separated into two sections A and B which were developed through information on the impact of risk management (RM), strategic decisions (STD) and corporate governance (CG) on organizational performance (OGP) of insurance companies in Nigeria as gathered from the insurer. Section A contains demographic, employee's status, educational level, management level and departmental information while section B is furnished with information relating to the study with three independent variables, risk management (RM), strategic decisions (STD), corporate governance (CG) and one dependent variable organizational performance (OGP). The variables features are clearly stated for easy description and recognition. The item designs of the questionnaire follow the 5-point Likert scale type ranging from '5 - strongly agree'; '4 - agree'; '3 - undecided'; '2 - disagree' to '1 - strongly disagree'.

A descriptive research design was adopted for the study. This gives the accumulated information gathered (Bryman & Bell, 2007). The study considered multi-sampling technique since the population of insurance companies in Nigeria is fifty–nine (59) and all the population could not be covered (www.naicom.gov.ng). So, for the purpose of the study, sixty percent of the population was considered which amounts to thirty-six (36) insurance firms and they were randomly selected using Lagos Headquarter offices. The questionnaire was randomly distributed for administering due to the nature of the study among four-unit heads of Compliance, Audit & control, Risk management and Accounting & Finance departments were taken into cognizance making a total of one hundred and forty-four respondents (144) in which one hundred and

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eighteen were returned (118). The statistical technique employed for this study was multiple regression at 0.05 level of significance.

The Analytical Model

This study followed the work of Kamau et al (2018) model but modified the variables as their study failed to take cognizance of risk specificity, which this study considered necessary. The model specification is stated in equation (1):

$$OGP = f(RM, STD, CCG)$$

…1

Where:

OGP (Organizational performance), RM (Risk management), STD (Strategic decisions), CG (Corporate governance)

Equation 1 is transformed into linear relationship as presented in equation 2

$$OGP = \lambda_0 + \lambda_1 RM + \lambda_2 STD + \lambda_3 CG + \mu$$

…2

Where:

λ_0 = Constant; λ_{1-3} = the coefficients of the indepent variables; OGP = Dependent Variable (Organizational performance of insurance company); RM = Risk Management; STD = Strategic Decision; CG = Corporate Governance; and μ = Error Term

Hypotheses

For the purpose of this study, three (3) hypotheses were generated. They are

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Hypothesis one

H_{01} - there is no relationship between risk management and organizational performance.

Hypothesis two

H_{02} - there is no relationship between strategic decisions and organizational performance.

Hypothesis three

H_{03} - there is no relationship between corporate governance and organizational performance.

Data Analysis Results and discussion

Table 1: Descriptive Statistics

Variables	Obs	Mean	Std.Dev.	Min	Max	p1	p99	Skew.	Kurt.
RM	118	20.203	4.807	6	30	6	30	-.405	3.551
OGP	118	18.492	4.402	0	27	8	25	-.981	4.66
STD	118	17.864	4.165	8	26	8	25	-.435	2.53
CG	118	19.288	4.036	6	25	9	25	-.952	3.617

Note: RM = Risk management, OGP = Organizational performance, STD = Strategic decisions and CG = Corporate governance.

Table 1 presents descriptive statistics for measures of organizational performance, risk management, strategic decisions and corporate governance and firm characteristics variables in terms of mean, standard deviation, skewness and kurtosis. Mean give indications on the average direction of the variables for each construct, while standard deviation provides information on the level of

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dispersion from the mean. A low standard deviation meant that most of the responses group around the mean. In addition, kurtosis and skewness was used to establish the measures of the shape of the distribution. The result in table 1 shows that risk management has a mean score of 20. 203 and standard deviation of 4.807. It has skewness of -0.405 making it to be negatively skewed to the left of the curve along with a kurtosis 3.551. The organizational performance as the dependent variable of the study, accounts for a mean of 18.492 and standard deviation 4.402. The curve is negatively skewed to the left with a skewness of –0.981 and kurtosis of 4.66. The other variables involve are strategic decisions and corporate governance that has mean of 17.864 and 19.288 with corresponding standard deviation of 4.165 and 4.036. Both are skewed to the left with skewness of -0.435 and -0.0952 and kurtosis 0f 2.53 and 3.617 respectively.

CORRELATION MATRIX OF THE VARIABLES (WITH SIGNIFICANT LEVELS)

Table 2: Pairwise correlations

Variables	(1)	(2)	(3)	(4)
(1) OGP	1.000			
(2) RM	0.593*	1.000		
	(0.000)			
(3) STD	0.470*	0.536*	1.000	
	(0.000)	(0.000)		
(4) CG	0.519*	0.448*	0.393*	1.000
	(0.000)	(0.000)	(0.000)	
*** p<0.01, ** p<0.05, * p<0.1				

In this study, pairwise correlation analysis was conducted to examine the relationship between the variables. The relationships among the dimension of risk management and organizational performance of insurance companies were

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examined (Schober et al, 2018). Cohen (1988) as cited by Wong & Hiew (2007) suggests the guideline for interpreting correlation coefficient value (r) that range from 0.100 - 0.299 is considered weak, 0.300 – 0.490 is considered medium and 0.500 – 1.000 is considered strong. However, Field (2005) suggested that correlation coefficient should not go beyond 0.800 to avoid multi-collinearity. The highest correlation coefficient in this research was 0.53 which is less than 0.800, indicating there is no multi-collinearity problem. The results displayed in table 2 demonstrates a significant and positive correlation exists between risk management and organizational performance (r = 0,593, p≤ 0.1), as well as corporate governance and organizational performance (r = 0.519, p≤ 0.1). Strategic decisions have a medium relationship with organizational performance (r = 0.470, p≤ 0.1).

Table 3: Linear regression

PERF	Coef.	St.Err.	t-value	p-value	[95% Conf	Interval]
RM	0.351	0.080	4.400	0.000***	0.193	0.509
STD	0.161	0.078	2.060	0.042**	0.006	0.315
CG	0.314	0.114	2.760	0.007***	0.089	0.539
Constant	2.480	1.271	1.950	0.054*	-0.039	4.998
Mean dependent var		18.492	SD dependent var			4.402
R-squared		0.448	Number of obs			118.000
F-test		73.220	Prob > F			0.000

**** p<.01, ** p<.05, * p<.1*

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Discussion of regression result

The result for goodness of fit test as represented in table 3 shows a coefficient of determination of R^2 = 0.448 (44.8%). This show that variation in the dependent variable OGP is explained by the independent variables (RM, STD, and CG) by 44.8%.

The p-value of the F- statistics is 0.000 which is significant at 5% explaining that the null hypothesis should be rejected. Consequently, the F- test as represented in the table shows clearly the fairness and non-biasness of the model. It also explains that the independent variables are significantly linked with the dependent variable.

Hypotheses Testing

H_{01} = there is no relationship between risk management and organizational performance.

The result of the relationship between risk management and organizational performance has a coefficient (r) of 0.351, signifying a positive link between the two variables with a p- value of 0.00 significant at 5%. This shows a positive effect of risk management on organization performance, we therefore, reject the null hypothesis which states that there is no significant relationship between risk management and organizational performance.

H_{02} = there is no relationship between strategic decisions and organizational performance.

From the result, the relationship between risk management and organizational performance has a coefficient (r) of 0.161, signifying a positive link between the

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two variables with a p- value of 0.042 significant at 5%. This shows a positive effect of strategic decisions on organization performance, we therefore, reject the null hypothesis which states that there is no significant relationship between strategic decisions and organizational performance.

H_{03} = there is no relationship between corporate governance and organizational performance.

From the result, the relationship between corporate governance and organizational performance has a coefficient (r) of 0.314, signifying a positive link between the two variables with a p- value of 0.007 significant at 5%. This shows a positive effect of risk management on organization performance, we therefore, reject the null hypothesis which states that there is no significant relationship between corporate governance and organizational performance.

The study conducted several statistical tests to fulfil the underlying assumptions of multiple regression analysis. These include, goodness of fit test, multi-collinearity and beta test. The study tested for linearity using ANOVA test of linearity. The result of linearity had a significant for linearity of $p < 0.05$.

Conclusion

The study was undertaken to study the relationship between risk management and organisational performance of insurance companies in Nigeria. This study uses primary data to examine the association between risk management variables and organisational performance of thirty-six (36) insurance companies in Nigeria. The result of the study shows that effective risk management, good strategic decisions and effective corporate governance will impact positively on organisational performance. The coefficient of determination is 44.8%. Though this relationship is not strong enough, there is the possibility of improving on

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this if more efforts are employed strategically to mitigate against the likely risk through proper identification of these risks and technically applying good corporate governance into the management of insurance business in Nigeria. This suggest that effective and efficient risk management play a determinant role in insurance industry's organizational performance in Nigeria. Where insurance company does not successfully control its risks or manage identified risk effectively and efficiently, its performance will be unsteady and the successful realisation of set goal(s) will be jeopardised. Regardless, the line of business risk management is important to business success and organisational performance. Business or organisation must focus on their corporate governance and strategic decisions taken to achieve organisational objectives.

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