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Rapid Currency Change in Zimbabwe: A Case of Harare Insurance Companies, Zimbabwe

Zingwina Moses*

Faculty of Commerce and Law, Zimbabwe Open University, Zimbabwe

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Abstract: The study investigated the effects of currency change within the insurance industry in Harare; Zimbabwe The research adopted the mixed research methodology. The objective of the study was to examine rapid currency management practices and their effects on performance of insurance companies. The research design was a descriptive survey. The study used interviews and surveys as data collection tools.. The study' findings revealed that insurance companies play a major role in safeguarding companies from collapsing by paying claims in the event of disasters. Furthermore players in the insurance industry were not willing to fairly design their products because of rapid currency change, thus poorly designed products flocked the market resulting in non payment of claims. The study recommended that Government of Zimbabwe through the ministry of finance should craft and implement monetary policies that do not cripple the operations of the insurance industry.

Keywords: Rapid Currency Change, Insurance Industry, Poor Insurance Products Design, Increase in Lawsuits Against Insurance Firms. Financial Records.

INTRODUCTION

Obasi (2010) describes insurance as a contract between the buyer of insurance and the insurance company which sells the policy. He further elaborates that by entering into the agreement, the insurance company accepts to pay the policy holder a preconceived amount out of money in the event of occurrence of a loss. According to Obasi (2010) Short term insurance refers to the period of insurance which is usually less than twelve months and risk is the variation of the outcome from the outcome that is being expected. Obasi (2010) assertion was supported by Oates (2017) who define risk as uncertainty that might happen and when it occurs, chances of loss or profiting are uncertain. Olifinnik (2010) stated that the principal goal of insurance is to transfer resources, from low marginal utility of income state to those where the marginal utility income is extremely high. The theories of insurance can best be explained by the principles of insurance. Olifinnik (2010) points out the following as being the foundations upon which the doctrine of insurance is built on outmost good faith, insurable interest, indemnity, contribution, subrogation, loss minimization and proximate cause. According to Olifinnik (2010) Insurable interest is the financial interest that the insured party has in the object insured, this means that for one to insure they should demonstrate that they will be disadvantaged should loss occur. He further explained Uberima Fidei as that parties to an insurance contract must disclose fully all facts that may materially affect the risk. This would mean that the insured has to disclose all facts that can increase or decrease the risk. Material facts influence companies to accept risk. According to Kozak (2011) argues that indemnity means that after the loss has occurred, the insurer should place the insured in the exact financial position they enjoyed before the loss. Indemnity is made in the following ways, cash payment, repair, replacement of reinstatement. Insured's are not supposed to profit from insurance and they also should not be made worse off after a loss has occurred. In a situation where two or more insurance companies are covering a similar event, should a loss occur the insurance companies must contribute towards the claim in proportion? Thus an insured cannot lodge claims from the two separate insures, otherwise that would violate the principle of indemnity. Contribution and subrogation are corallines of indemnity. Olifinnika (2010) the two principles work in such a way that indemnity. Subrogation entails that the insurer steps into the shoes of the insured after having paid off the claim. It mainly works in motor insurance where the insurer claims their settled amount from the guilty party. Proximate cause means the actual cause of a loss. These are referred to as excreta payments, meaning they are paid out of grace. Insurance companies might want to maintain good relationships with clients hence they would pay for claims. According to Kihara (2011) in the insurance industry, underwriting is the process used by an insurance company to determine whom to insure and the adequate premium to charge which will be commensurate with the risk.

Insurance companies should collect more premiums than the amount that they pay out in claims.

This enables the insurance companies to make money from the invested premiums.. Change of currency (demonetization) refers to the change of currency status as a legal tender, which means replacing old notes or coins into new ones. The opposite of demonetarization is remilitarization which means restoring the demonetized currency as a legal tender. According to Oates (2017) the major reason why it is done is to eradicate inflation, corruption and other crimes, tax evasion, counter faring, to discourage the cash dependent economy and to facilitate trade.

The change of currency has different positive effect as this help the government to destroy corruption, tax evasion and black money. It also helps to slow down the unaccounted which is kept by the public in their bank accounts. Through demonetization the government help to put an end to the people who are involve in doing illegal activities such as gambling. It can also help the people to deposit their incomes in bank which can provide a good amount of tax, infrastructure, hospitals, educational institutions and many other facilities.

However according to AIO (2010) this has negative or disadvantages such as affecting small business firm to incur huge financial losses temporarily. Due to inadequate supply of notes people are faced with a lot of problems. Business can also be affected by as the currency changes might result in inflation rising within the country.

It is not debatable that when there is demonetarization the financial crisis becomes so high within the country. This in turn will have an impact on the insurance industry. Thus it is important to have a look on how the industry is negatively and positively affected. According to AIO (2010) the financial crisis has a visible impact on the insurance industry, primarily through investment portfolios, as the crisis spread and the financial market valuations and the outlook for real activity deteriorates. According ZARO (2015) the financial crisis can primarily be termed as a banking crisis and as insurance industry representatives have regular emphasized, the solvency of the insurance sector as a whole does not appear to be threatened. Nonetheless companies from that sector have been affected, and in mostly adverse ways. Forum (2013)) argues that a number of concentrated exposures to credit and market risk have been reviewed. Beyond these immediate issues related to the financial health of insurance sectors and companies, the crisis has clearly demonstrated that protection against systemic risks should also include monitoring and mitigating risks in the insurance sector and companies.

Even though, the evidence available so far suggest that the role of the insurance function in the financial crisis has had a stabilizing rather than a destabilizing influence on the system as a whole. Hifzam (2014) argues that the financial has largely resulted in the industry being unstable as opposed to the stability that is purported. Insurance companies are large investors especially life insurers and they have long term investment horizons than several other financial institutions such as banks. They have the capacity to hold a relatively large part of their investment to maturity, which help the system withstand short term shocks. In contrast some other types of market participants have had to sell into falling markets as a result of leverage, liquidity, regulatory and other considerations.

With this said the picture is not as rosy if one zooms from the aggregate picture into specific segments of the insurance sector. In the case of a number of insurance companies, especially those involved in activities traditionally associated with investment banks, valuation and rating pressures have been significant. According to Kaguri (2013) these pressures, in turn, have had repercussions that have tended to amplify downward pressures in financial markets during the crisis. Perhaps the most egregious example is afforded by the financial guarantee insurance sector, where subsequent downgrading of the various entities operating in this sector led to waves of downward pressure on market valuations of the securities wrapped by these entities and present in the portfolios of many other financial institutions.

Such activities cause imbalances and hence the crisis. According to Oates (2017) financial guarantors elevated the credit ratings of complex, structured financial instruments, making these products attractive to more conservative investors including the insurance companies. According to Krawis (2013) also the participation of insurance companies as counterparties to investment and commercial banks in credit default swap transaction enabled the latter to hedge their credit risks, thus permitting them to continue to expand their securitization activities, including in the form of collaterised debt obligations involving subprime mortgage related debt.

What is often les noted I the fact that the financial instruments used in the massive credit risk transfer prior to the financial crisis have had their core in many cases insurance like innovative financial instruments, that is credit default swaps. Krawis (2013) argues that, granted, insurers themselves may not have been frequent counterparties to these transactions, as the capacity of these companies to engage in such transaction is severely restricted by regulation. But the crisis has shown none the less that, despite such constrains, some types of insurance company’s actually accumulated significant exposure to credit default derivatives on one or the other side of their balance sheets.

***Corresponding Author:** Zingwina Moses

Sekarah, Y (2016) carried out a study to examine and identify the factors affecting the financial performance insurance companies during the period 20012 to 20017 and it was largely noticed that liquidity plays an important role in the management competence of a company especially when it is understood as an independent value. Hifzam (2014) investigated the factors that affect the financial performance of insurance companies and they also came to the same conclusion that liquidity plays an important role in affecting the insurance sector. Liquidity from the context of insurance companies is a measure of the ability of an insurance company to pay liabilities such as payments of loses and benefits under insurance policies which fall in a period less than a year. According to Kozak (2011) thus having assets to cover liabilities is crucial as people can make claim at any time or there might be a national disaster causing large number of claims resulting in the company paying out large sums of money. Thus companies with more liquid assets are likely to fail because they can realize cash even in very difficult situations. The issue of liquidity is directly related to the issue of demonetarization. According to AIO (2010) the change of currency increases in the country the liquidity rate of insurance companies falls resulting in the companies being unable to pay out premiums to their valued clients. Companies with more liquid assets are less likely to fail because they can realise cash even in difficult situations. It is therefore expected that insurance companies with more liquid assets will outperform those with less liquid assets. Kihara (2012) provides evidence that performance is positively related to the proportion of liquid assets in the asset mix of insurance. This clearly reflects that liquidity plays an important role in the insurance sector. However, as a variable it is directly affected change of currency hence it becomes such an important factor in affecting insurance industry. The rate of inflation typically refers to changes in the overall level of prices within the economy. Few authors have documented the impact of the inflation rate on the non-life insurance industry. AIO (2010) argues that deflation and inflation each present significant risks to the insurers. Some scholars argue that payment of premiums by clients does not reflect inflation. However, payment of claim by a company reflects inflation for example the value of an asset insured might change price as a result of inflation resulting in the insurance company paying more. Kaguri (2013) analysed the performance of non-life insurers and found that macro-economic conditions indicators such as inflation and income inequality influence the performance of companies. According to Olifinnik (2010), inflation results in the financial stability of the entities being affected. Thus the issue of inflation directly has an impact in the insurance industry. However, it should be noted that the inflation is accelerated by demonetarization within the country. Thus it is no doubt that the impact of inflation is correlated to the change of currency within the country.

Leverage is measured by the ratio of total debt to equity; it shows the degree to which a business is utilising borrowed money. According to Kaguri (2013) leverage is an important instrument in ensuring the survival of the industry. Companies that are highly leveraged maybe at the risk of bankruptcy if they are unable to make payments on their debt, they may also be unable to find new lenders in the future. Insurance companies could prosper by taking reasonable leverage risk or could become insolvent if the risk is out of control. According Kaguri (2013) if a firm is profitable then it I more likely that financing would be from internal sources rather than external sources. In other words, firms tend to use internally generated funds first and then resort to external financing. Through the change of currency, the capital flows resulting in proliferation of many insurance companies. The short term insurance industry has too many players whereas business is very low an evidenced by the low technical rates insurance premium rates, density and penetration.

However, the stabilisations benefits, in the multi-currency regime seem to have eluded the insurance sector as currently too many players are chasing a very small scale. According to IPEC (2012) through the demonetization of the economy most of the premiums were then settled not in cash but on credit which then shows that the change of currency has a negative impact on the insurance sector. This situation has resulted in exorbitant premium currency hence poor services end up being provided by the insurance companies to the policy holders.

Moreover, the insurance underwriters as real activities are declining as which will then adversely affect the insurance sector. Due to these impacts the insurance sector is bound to be affected by an increasing fraud land activities. The economies potential to create insurable risk remains lazy as the following factors are militating against the potential, low capacity utilization, low rates of liquidity and capital accumulation, Zaro (2015). Meaning lack of funding as a result of change of currency has left the companies in dire need for capital to fund them. Hence the sector will need deep pockets in order to deal with meaningful risk. According to IPEC (2011) the companies they end up competing on two dimensions that is price and service quality; though in Zimbabwe there I hardly any product variation with all those offering the same basic no frills product. On the same note the effect of the liquidity crisis are still being felt and the business remains, unattractive and such a context give rise to unfair and destructive competition in the insurance market marked among others by a disastrous underrated risk.

The liquidity can also affect the exchange rate. According to Kaguri (2013) the liquidity will be referring to changes in theoretical level of prices within

***Corresponding Author:** Zingwina Moses

the economy. Underwriters profits are over related to with the inflation rate, deflation and high inflation each present significant risk to insurers. However, payment of premium does not reflect inflation. Payment of claims by a company might reflect inflation for example the value of an asset insured might change prices a result of inflation resulting in the insurance company paying more. Krawis (2011) agree with the same notion that in this crisis the end result will be the insurance company being affected. According to Kaguri (2013) liquidity is also an important determinant of financial health of insurance companies and they have a negative relationship. So in this case since the liquidity crisis is caused by the change of currency then it became an in fact effect to the survival of these firms within the insurance sector.

In addition, we can also note that the sector has even been affected in terms of its stakeholders. According to Kaguri (2013) the rapid change of currency has resulted in some insurance companies raising their premiums to such an extent that individuals can no longer afford to pay the premiums. This means that both the company and the other stake holders are then deeply affected. One can note the subsequent rise in premiums will result in loss to those being insured as this means that they can no longer continue getting cover and at the same time not being able to be refunded by the insurance companies as the principles stipulates. This means a continuation in the shifting of currency will they be a blow to the industry. Talking of investors, even under such an economy investor might find it difficult to take part in the growth of the sector as they lose confidence as a result of the situation at hand. According to Obasi (2010) a positive for the insurance company is that they are typically funded by a relatively stable flow of premiums, with very limited chance on short term market funding, of which lowering any rating can downgrade can trigger collateral calls. This then shows that they are highly protected during times of turbulence.

The different stakeholders within the industry include the owners of the insurance firms and the workers together with the managers. The industry when it is affected even these people are adversely affected by the change of currency within the industry. To begin with, owners of the firms it should be acknowledge that when this phenomenon happens these owners suffers as they risk losing their investments in the face of demonetarization in Zimbabwe many company owners have faced the risk of liquidating their firms not only in the insurance sector but even in the whole business environment. According to Obasi (2010) the owners have suffered and at the same time they have also ripped benefits from there demonetarization process. One can note that in times of this crisis some take the advantage of their clients by scaling up their prices to an extent that they can either give up their premiums then they reap profits from the situation. Some they even take their time to falsify their company status by publishing false account statements which in turn make their companies look lucrative to investors.

Workers as the stake holders also get affected by the situation as the situation results in their covers being affected. If the firm cannot cope with the existing business environment the workers also suffer the risk of being laid off. Sekarah (2016) it is also much common that if the firm is still small its chances of survival are slim in an environment where there is constant change of currency. Since these companies will be facing liquidation and their continuity uncertain chances that the workers will lose their jobs are high. Even their incomes within this business environment remains affected as sometimes the companies might not be able to keep pace with the inflation that will be accelerating at such a high pace. It is also important to note that this high rate of inflation keeps on affecting the standards of living of the workers which then degrades the progress of the firms in terms of employment.

The major externally affected stakeholders include the public. According to Kaguri (2013) the external stakeholders plays a central role in ensuring the legitimacy of the insurance industry. The insurance industry has suffered in terms of its external stakeholders as a result of demonetarization. The industry is always changing its monthly premiums and as a result the public is always affected. It is really difficult for them to know which currency to legitimize and also to give their clients a fixed monthly premium they are supposed to pay. This then largely affect the public, omen people are forced to abandon their premiums as a result of this. They are in other words forced to discontinue paying them premiums and rich living lives which do not have them covered from risk that might affect them. According to Kaguri (2013) the matter is not only in the public having their premiums being terminated but some also risk losing their money that they would have paid for security in the old age. Taking into account how the insurance sector operates. In the end the public as a stakeholder then loses much as a result of demonetarization.

It should also be considered that during these times the public also suffers from manipulation of accounts statements of these firms. Even though the companies might be facing liquidation they always continue to mislead the public. According to Kihara (2012) this then results in the public rushing for premiums without taking into account how the companies are copying out in the business environment. Since they do not have the ability to obtain first and truthful information chances of being misled are high and they will always remain on the suffering side.

. Thus main objectives of local Insurance companies are to cover risk when they occur. A study of Insurance Companies in Harare, Zimbabwe is therefore critical given their immense contribution to country through covering of risk. In addition, government policies can also be taken into account, when switching currencies. Government has to come up with ways which also insure that the sector won't be entirely affected like reserving their money through the central bank so the government should have an act with the insurance sector which protects them in times like these. It also is important for the insurance sector as an industry to protect its clients. Because the real truth is that the sector benefits more in times like these hence the need to protect its customers. There should be a way through which the sector should insure that the premiums a fixed such that there is no rapid rise of prices which only benefit one side. In order to survive the issue of demonetarization companies can count on equity capital. This is referred to as the capital rose from the owners of the company. The more the capital the more the firm can grow accompanied by economies of scale and hence improved financial performance. An equity returns increase, return on an insurer's investment portfolio may also increase and this may improve the performance of insurance companies. Kaguri (2013) has the view that equities have the benefit of providing inflation hedge over the long term. Moreover, a higher proportion of investment in equities could lead to a higher risk of insolvency if the values of the assets dropped. Thus if insurance companies aim to survive they are supposed to take into account the impact of equity capital in their long term goals. The firms can only grow and multiply that's if equity capital is taken into account.

Since the liquidity risk is also one of the major issue that has an emerged as a result of the issue of demonetarization. This in the past had not been taken into account and hence there is need to pay attention to the impact that this will have on insurance companies. Thus insurance companies should start to take a serious note in terms of managing the liquidity issue which stems from the change of currency.

EXPERIMENTAL SECTION/ MATERIAL AND METHODS

Statement of the Problem

Rapid currency change with no law to protect the insurance sector has led to wrong assumptions that insurance sector is a risk sector to invest in, resulting in poorly designed products flooding the market, non payment of claims among other problems. What is the rationale of running an insurance sector where poorly designed products are flocking the market and non payments of claims are the order of the day despite premiums being paid?

Objectives of the Study

To examine rapid currency management changes practices and their effects on performance of Insurance Sector, based on a study of hundred (100) insurance sector staff, in Harare

Research Question

Do the issue of rapid currency change on Insurance Companies in Harare, Zimbabwe has a major effect when investors when they want to enter into contract with insurance companies?

Methodology

The population of the study consisted of 100(hundred) members from Harare, Insurance staff drawn from managerial, accounting, auditing and policy holders in Harare Insurance companies A mixed method approach was used to assess the main cause of poorly designed products flooding the market as well as non payment of claims by insurance companies.

A purposive approach to select 35 (thirty) members was used for the study as it enabled the researcher to consciously select a sample appropriate for the Study .In-depth interviews that allowed respondents to answer certain questions in order to secure desired information and questionnaires were the data collection tools in this study.

RESULTS AND DISCUSSION

The study wanted to find out effects of demonetarisation on Insurance Sector basing on poorly designed products flocking the market and failure to pay claims despite policy holders paying huge premiums. . The following results were obtained.

Table 1. Effects of Demonetarisation on Insurance Sector

Challenges	Agree	Not Sure	Disagree
Do you encounter loss of clients?	80%	5%	15%
Is there issue of financial crisis ?	85%	5%	15%
Is there inadequate knowledge by insurance underwriters?	90%	5%	5%
Do you encounter liquidation of entities?	80%	2%	18%
Retrenchment of workers common?	90%	5%	5%
Does inflation has effect on rapid currency change?			

Source: Primary data 2021

The majority of respondents agreed (80%) that there is loss of clients on insurance companies as a result of demonetarisation of Zimbabwe Currency, with a minority in disagreement (15%) and (5%) not sure.

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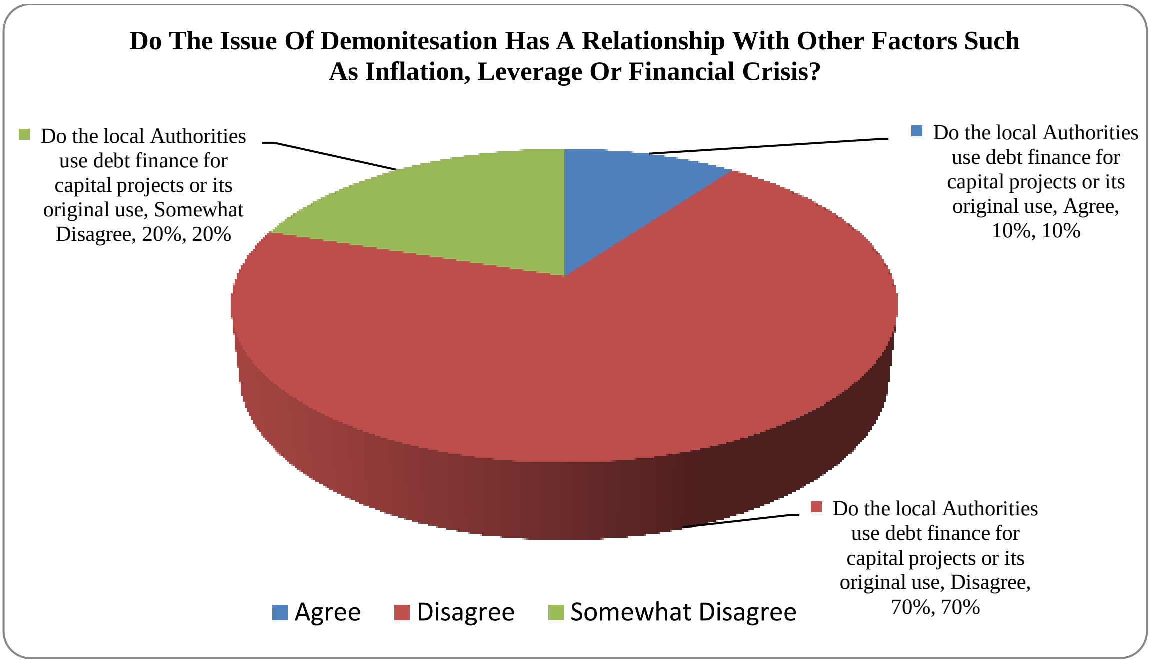
In- depth understanding of Insurance companies, in Harare Zimbabwe and effects on demonetisation provided by the respondents included, loss of clients, financial crisis, liquidation of insurance companies among other problems.

Do The Issue Of Demonetisation Have A Relationship With Other Factors Such As Inflation, Leverage Or Financial Crisis?

The research intended to establish whether demonetisation has a relationship with other factors such as inflation, leverage or financial crisis. The following results were obtained:



Source: Primary data 2021

Interviews data gathered with the Insurance companies indicated that there is a link (70%) between demonetarisation and three variables namely inflation, leverage and financial crisis. Authorities members indicated that they were aware of the obligation of insurance companies, in Harare, and requirement that the insurance companies must meet their other side of the contract for example payment of claims when due and not giving clients poorly designed products .One of the informants said "*…it is reasonable given that the ability of an Insurance companies to pay claims when due depends to the large extent rapid currency change in Zimbabwe.*

Moreover, data gathered through questionnaires concurs with data collected from interviews. Thus, this shows that the respondents were aware of major effects of demonetisation facing them, loss of clients, non payment of claims when due, liquidation of insurance companies among other problems

Rapid currency change directly influences the financial performance of an organisation or entity as they determine key financial variables such as returns, risks, cost of capital and market price of insurance product. The major aim of organisations is to make sure that their clients are satisfied. A proper policy management system and proper staff training in underwriting debt are key factors that influence company performance and recommend whether the company should enter into short or long contacts with its clients.

Insufficient knowledge of quality insurance products debt has led to wrong assumptions that all insurance companies offer poorly designed products.

FINDINGS

The study revealed that policy holders and other external investors require proper management of funds (premiums) and first class service in terms of claims settlement delivery by Insurance Companies, thus it complies with the understanding at the continental level. The Insurance companies were not able to give proper service delivery because of inadequate knowledge of contract they entered and also issue of rapid currency change by debt management personnel and political interference by councillors.

CONCLUSIONS

The study concluded that insurance companies must fulfil their side of contract and must lodge for a law that protects them in case of rapid currency change. Financial performance of Insurance Companies must not be hindered by lack of knowledge by insurance personnel and rapid currency change.

***Corresponding Author:** Zingwina Moses

Recommendations

The study recommended that Government of Zimbabwe through the ministry of finance should craft and implement monetary policies that do not cripple the operations of the insurance industry.

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