

## **Economic Growth and Insurance Sector Development of Sri Lanka**

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### **Introduction**

Financial systems are an important element for the economic growth process, because they have a function which provides funds for wide spreading of new technologies and accumulation of capital funds. Insurance serves a number of valuable economic functions that are largely distinct from other types of financial intermediaries as it provides risk transfer and compensation by the efficient distribution of different risks. A well-developed insurance sector is necessary for the economic development of an emerging economy like Sri Lanka, as it provides long-term funds for physical and social infrastructure, while simultaneously strengthening risk-taking abilities. The increase of total assets by 22%, income by 40% and pre-tax profit by 262% shows the expansion of Sri Lankan insurance business in 2010 (Central Bank of Sri Lanka Annual Report -2010). This study examined the current industry conditions of insurance industry in Sri Lanka and was focused on assessing the relationship between economic growth and insurance sector development. Further, to focus on the causality directions between two identified variables also was a main objective of this particular study.

### **Methodology**

The study was totally based on the time series data. Data were collected mainly through secondary sources for the period 1997-2010. The data were mainly gathered from annual reports of Insurance Board of Sri Lanka and annual reports of Central Bank of Sri Lanka. In defining the variables, total premium (TPREM) earned by the insurance businesses was used as the predictor of insurance sector development and economic growth was predicted by a broad set of control variables such as Capital Expenditure (CAPITAL), Labour Force Participation Rate (LABOUR), Broad Money Supply (MS), and Direct Investment (DINVEST) other than Both descriptive as well as econometric analysis were performed for analyzing data. Main two inferential techniques were used in analyzing data. A multiple regression model was tested to capture the relationship and strength of the relationship between insurance sector development and economic growth and Granger Causality Test was performed to identify the causality direction of this relationship flows.

### **Results, Discussion and Conclusions**

Results indicated (Table 1) that all the independent variables except money supply have a positive relationship with the industry growth and all the independent variables except labor force participation and direct investment were significant at 5% confidence level. The scenario led to conclude that there is a positive relationship between two variables in Sri Lankan context.

According to the Table 2, direct investment only has one way causality direction. All other variables had not clear causality direction with industry growth even the most important variable called as total premium earned by the insurance businesses is also had not clear causality direction with the dependent variable.

Table 1: Determinants of economic growth and industry performances

Dimensions	B	P value
Constant	17.0163	0.0001
Log(Labour)	0.0408	0.9472
Log(Capital)	0.0615	0.0194
Log(Dinvest)	0.0217	0.8156
Log(MS)	-0.3351	0.0228
Total Premium	0.0092	0.0480
@ Trend	0.1538	0.0002

Table 2: Analysis of granger causality

Null Hypothesis:	Obs.	F-Statistic	Prob.
LOG(LABOR) does not Granger Cause LOG(GDP)	14	0.41933	0.6786
LOG(GDP) does not Granger Cause LOG(LABOR)		0.56114	0.6028
LOG(CAPITAL) does not Granger Cause LOG(GDP)	14	1.59086	0.2920
LOG(GDP) does not Granger Cause LOG(CAPITAL)		1.80917	0.2564
LOG(DINVEST) does not Granger Cause LOG(GDP)	14	4.02764	0.0908
LOG(GDP) does not Granger Cause LOG(DINVEST)		0.37952	0.7023
LOG(MS) does not Granger Cause LOG(GDP)	14	0.59987	0.5841
LOG(GDP) does not Granger Cause LOG(MS)		0.00516	0.9949
TPREM does not Granger Cause LOG(GDP)	14	3.11580	0.1322
LOG(GDP) does not Granger Cause TPREM		2.33681	0.1921

### Conclusions

A clear positive relationship was observed between economic growth and industry performances in Sri Lankan context. Further, the industry performances are highly sensitive for the identified economic dimensions.

### References

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