

Chapter 26

Insurance as an Optimization Tool for Risk Management in Small and Medium-Sized Enterprises

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ABSTRACT

The SME risk management optimization model includes appropriate methods for identification, analysis and classification of risk assessment and developing a plan to overcome the risks and control the applied reaction to risk. Insurance is a classic way of a risk management process and is applicable to specific situations. The subject of this study is exposure and risk management in small and medium-sized enterprises (hereafter: SMEs) which are eligible for transfer of insurance coverage. This paper discusses the process of risk management in SMEs by transfer to insurance and indicates which risks and in what way can be transferred to the insurer. In this paper we analyze the supply of domestic insurers in Serbia, and insurance requirements, variants that offer coverage to overcome the particular risks to which SMEs are exposed. In the elaboration and research of mentioned theses the paper will use methodological procedures of analysis and synthesis, the inductive-deductive method, and if necessary, the comparative method of scientific research.

INTRODUCTION

The purpose of this chapter is to analyze the risks which SMEs transfer to insurance companies, and the value of risk optimization management in these businesses. The underlying premise is that SMEs in Serbia fail to manage risks in an optimal way. The chapter starts from the premise that SMEs have difficulty in understanding insurance products, and that they need both support and assistance in this regard. In this sense, the chapter deals with main characteristics of insurance, with the aim to show how

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SMEs can optimize risk management and what the role of insurance companies could be. In an effort to identify issues that occasionally arise and point to possible solutions the author will compare the experience of countries with an advanced insurance market for SMEs, Great Britain and Australia in particular, with that of Serbia. Experience shows that in advanced economies insurance market is very competitive. Next, the chapter will examine offers of insurance products in the Serbian market and the use of broker insurance services. To enhance this chapter, the author will consider issues of importance to SMEs using as an example insurance services in Serbia and possible differences in relation to countries in which there exists a developed insurance market. Insurance sector examples will be presented to support the approach, but the focus will be on opportunities for SMEs. Following the above main content, the chapter discussion will include future research directions. Finally, the chapter ends with a conclusion and key terms and definitions.

BACKGROUND

Small and middle sized enterprises (SMEs) are considered the key drivers for growth and development of national economies. They contribute to growth of employment, particularly in the sectors of transport, civil engineering, communications and tourism. (Jeremić, Živić, 2011, p. 78) For example, in United Kingdom SMEs play a vital role in the health of the economy and according to the Financial Conduct Authority (2015) “99.3% of private sector businesses are SMEs.” Similarly, in the Serbian economy 99.8% of business entities are SMEs (Chamber of Commerce and Industry of Serbia, 2016).

SMEs are exposed to numerous business risks. Most organizations must take risks in order to develop, so not all risks are inherently a negative phenomenon (Udovičić & Kadlec, 2013). SMEs regularly face certain threats and numerous risks which endanger their operations. This can have unfavourable economic consequences. Exposure to risks, especially negative ones, must be taken into account also in good times, when profits are increasing (Simons, 1999). SME business success depends on decisions concerning protection of particular risks and measures that should be adopted in order to control and reduce risks. In that respect, quality management of each company includes the organization of monitoring and management of risk.

Realizing SME significance the Boston Consulting Group carried out an extensive survey of 2,500 small businesses in six largest SME insurance markets: U.S., UK, Italy, France, Germany, and Japan. The research explored the insurance decision-making processes of small business owners and found that SMEs are more open to direct interaction and outreach from insurers than many experts have expected. SMEs expect targeted outreach initiatives, improved value proposition for brokers and agents and a “*hybrid direct*” model that provides semi customized offerings, advice, and information (Hoying, Agarwal, Rapsch, & Yasushi, 2014).

At a time when businesses, particularly SMEs, face the consequences of the economic crisis and climate change increases the frequency of extreme events, it is important to discuss issues related to security as a model for overcoming the risks to which SMEs are exposed. Insurance provides a certain amount of security in terms of decrease of potential loss that may occur through realization of risks covered by the insurance. The main objective of risk optimization in SMEs, especially after the occurrence of adverse events, is to establish at least a minimum of business activities in the shortest possible period of time (Njegomir, 2011, p. 41). The additional benefit is that an insurer provides support to SMEs, stimulates better and safer SME operations.

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