

### **Capítulo 3**

## **A the orethical analysis of strategic alliances in the mexican insurance market**

José Vargas & Edgar Ruiz

J. Vargas & E. Ruiz

University Center for Economic and Managerial Sciences

Universidad de Guadalajara, Periférico Norte 799 Edif G201-7, Núcleo Universitario Los Belenes,  
Zapopan, Jalisco, C. P. 45100; México

[jvargas2006@gmail.com](mailto:jvargas2006@gmail.com)

M.Ramos, M.Miranda (eds.) *Estudios en Finanzas y Contabilidad: España y América Latina. Estado del arte y las nuevas metodologías aplicadas*, Temas Selectos de Finanzas-©ECORFAN-Madrid, España, 2013.

## **Abstract**

The aim of this work is to give a perspective about the utility of the strategic alliances from the view of three theories: The resource-based theory, the industry-based theory and the institutional-based theory. The raised hypotheses were that the strategic alliances are useful to enter to the markets, growth and expand a firm. The methodology used was exploratory data analysis of the insurance sector and the top five insurance firms in 2011. It is concluded that the strategic alliances are reflected the insurance market of México having strong implications at the three levels local, industry and institutional.

**Key words:** Foreign investment, Mexican insurance companies, strategic alliances, strategic resources.

## **3 Introduction**

Talking about security in Mexico, it can be realized that is an area where development is not yet well entrenched culture toward insurance. Very low percentages of the population have insurance of various kinds. For example only 5% of homes are protected from disasters and not all cars are insured as indeed happens in other countries (GNP, 2012). Because of these conditions, the Mexican insurance industry is a constant growing market both in sales and services as new entrants. So the numbers point to a more competitive market (CNSF, 2011).

That said the leading theories in strategy are suitable to explain how firms interact with other businesses to find success in the market mentioned above. This research addresses three main theories to explain the behavior strategy of the insurance industry. They are the resource-based theory, the industry-based theory and the institutions-based theory. In addition, strategic alliances are useful from the point of view of each of the theories proposed. This is because they allow the production of resources, when talking about the firm, to compete and cooperate at the industry level. Strategic alliances also allow exploring new markets through institutional requirements in each country (Peng, 2007).

### **3.1 Definition of the problem**

The five leading theories on strategy have arguments for the formation of strategic alliances. The transaction cost theory and agency theory have found that strategic alliances reduce transaction costs leading to greater efficiency and reduced costs of governance. However, these two theories do not focus on strategy and social factors (Eisenhardt & Schoonhoven, 1996).

Zervos (2004) studied the transaction costs of debt and equity issuance for firms in México and concluded that Mexican firms issue debt at the lowest costs and at the highest equity issuing costs. Institutional investors including insurance companies are less involved with equity and more involved in private company debt. The insurance companies in México are regulated to manage long term debt instruments investing an important share of their assets in foreign values and stock.

While the resource-based theory, the industry and institutions based theories clearly highlight the collaboration between firms and strategies that are made for competitiveness, growth and exploration of new markets.

This research is more focused on exploring strategic alliances as a means to compete, grow and expand into the insurance market in Mexico. For this reason this analysis takes the position of the last three leading theories on strategy. This research is limited to analyze the dynamics of the insurance industry in Mexico at the end of the year 2011

Finally, the formulated research questions are:

- a. Are strategic alliances means to obtain resources and to improve competitiveness of companies in the insurance sector in Mexico?
- b. Within the insurance industry is present the phenomenon of cooperation and competition seen between all businesses together?
- c. Does the formation of partnerships have facilitated foreign investors entering the insurance industry in Mexico?

### **3.2 Justification of the problem**

According to quarterly sector analyzes of the National Commission of Insurance and Finance (Comisión Nacional de Seguros y Fianzas) from 2001 to 2011 (CNSF, 2011). The insurance market in Mexico is a growing market, both in business, sales and service. Similarly, the insurance market turns to a more competitive market. So the role played by strategic alliances is crucial for companies in this market and it is consistent with the three theoretical approaches proposed.

### **3.3 Hypothesis**

The three hypothetical scenarios that can be found out are the following:

- a. In the insurance industry strategic alliances at the company level are used to obtain resources and compete successfully.

- b. Partnerships are a phenomenon of competition and collaboration between companies in the insurance sector.
- c. Through strategic alliances many foreign companies have managed to enter the insurance sector in Mexico.

### **3.4 Objectives**

The overall objective of this research is to give an overview of strategic alliances and the important role they play for local business, industry and institutions. The particular focus is to analyze strategic alliances in the Mexican insurance sector from the point of view of the three theories proposed.

### **3.5 Schematic references**

#### **3.5.1 Conceptual framework**

Next we define some important terms for the development of this research.

- a. ***Strategic alliances.*** A strategic alliance is an agreement between two or more firms to share exchange or develop products, technology or services (Gulati, 1998). Partnerships and strategic alliances can be subdivided into contractual and capital a strategic alliances and partnerships. Contractual alliances are the type of alliance that is not based in the capital. They serve for joint marketing, research and development (ID) contracts, projects ready to operate, strategic suppliers and distributors and strategic licensing and franchising. Based-capital strategic alliances and partners include investment capital of a partner over the other and vice versa. A joint venture (JV) is an example of capital strategic alliance and partnership. It occurs when a new entity is formed from two or more investment companies.
- b. ***Strategic networks.*** They are strategic alliances composed of multiple firms to compete against other similar groups and against traditional individual firms. Strategic networks are known as constellations (Das and Teng, 2002).

#### **3.5.2 Theoretical framework**

In this section it is introduced and explained the formation of strategic alliances on each one of the three theories confined in this investigation.

- 1). Resource-based theory: The resources and capabilities-based theory explains that the company's competitive advantage is based on the allocation of owned resources and efficient use given to them. Barney (1986) notes that the creation of non-homogeneous and differentiated goods forms the basis for a company to

have a competitive advantage, or whatever it is, get greater benefits than under perfect competition. The cause of non-homogeneous products is explained because firms are heterogeneous resource endowments (Barney, 1991). And as suggested by Wernerfelt (1984) resources and products are two sides of the same coin, leading to the creation of differentiated products.

To classify a resource as a source of competitive advantage, this can be supported by the model of Barney (1986). The model consists of four characteristics that must be met to be considered a strategic resource or source of competitive advantage:

- Valuable
- Rare
- Imperfectly imitable
- Imperfectly substitutable

The relationship of the theory of resources and strategic alliances is as follows. The firm needs resources to sustain a competitive advantage. These are not traded in factor markets and cannot perfectly imitate or substitute (Barney, 1986). So the company has two options, either to internalize meaning developing within the organization or to form an alliance to access them (Grant and Baden-Fuller, 2004). However, strategic alliances and partnerships have the advantage of being less expensive and resources are obtained faster

## 2). Theory based on the industry

The vision based on industry approached companies as independent players to maximize their performance. The truth is that within an industry companies are involved in various relationships of competition and collaboration (Gulati et al 2000). So it makes sense to talk of strategic alliances from the framework of Porter's five forces (Porter, 1996).

- First, the rivalry between firms reduces profits. So, instead of competing, firms form strategic alliances, known as vertical alliances. Sometimes the goal is to stop a potential competitor (Peng, 2007).

- Second, suppliers are seen as threats. However, by working with these, called vertical alliances up, they have the advantage of obtaining larger and longer contracts with fewer suppliers and increase the bargaining power and incentives to make more investments to improve the products (Peng, 2007).

- Third, buyers are another threat. But together with these and distributors, known as downward vertical alliance, it has the benefits of being able to reach more customers (Peng, 2007).

Finally, the entry of a substitute product requires the formation of strategic alliances and partnerships to realize the potential of this new product (Peng, 2007).

3). Theory based on institutions: Formal and informal institutions are known as the rules of the game, and are those who are responsible for regulating strategic alliances (Peng, 2007).

Formal legal frameworks and regulatory have an impact on two aspects of the strategic alliances:

a) There are antitrust laws primarily alert when two rival firms try to form an alliance. In some countries are prohibited mergers and acquisitions because they remove a competitor, whereas the less tight alliances are allowed (Peng, 2007).

b) The requirements on the input mode. Some governments prohibit the procurement and only allow strategic alliances and partnerships with local businesses as the only means of entry for foreign direct investment, allowing them to be shareholders only a percentage of total capital. In recent years many governments have implemented policies that give more freedom to the entry of foreign capital and even some countries now allow wholly owned subsidiaries (Peng, 2007).

c) Contextual framework: the insurance market in Mexico

1) Structure

Mexico is the second largest in Latin-Americans insurance markets the emerging Mexican insurance market has a penetration index of around 2% of GDP. After the privatization process during the period 1986-1992 (Tamez, Bodek & Eibenschutz, 1995) and before the North America Free Trade Agreement (NAFTA), growing of medical insurance market was following the tendency of grow of medical services in private sector (Laurell, 1994). During this period, the Mexican government promoted reforms and decrees to privatize, opening and modernize the insurance industry aimed to achieve a greater competitiveness and efficiency of the sector.

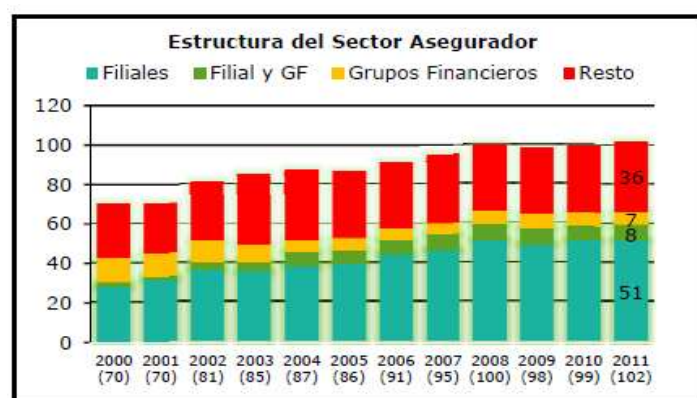
These economic and financial reforms of the new General Law of Institutions and Mutual Insurance Societies eliminated the barriers allowing the participation of foreign direct investment in the social capital of insurance companies operating in México (Ruíz-Ramírez, 1992; Asociación Mexicana de Instituciones de Seguros A. C. Sector Seguros, 1991).

Currently insurance companies conduct trading businesses operations involving similar financial instruments and counterparties subject to different capital regulations.

Capital regulations on insurance companies are based on a consolidated basis to consider their liability structure. Liabilities are considerably longer, difficult to value and typically not tradable financial assets for insurance companies. For most insurance firms operating in the market forces, the dominant role in decisions of capital is not subject to minimum regulatory requirements (Herring and Schuermann, 2003).

Despite that the premiums and the market are growing, the expansion of the insurance market is constrained by competitive pressures among more than 60 companies. Therefore the level of penetration is low. At the end of 2011, according to reports from the Insurance and Surety Commission (CNSF, 2011) the insurance industry ended the year with 102 institutions. Of these, 15 were incorporated into a financial group, 59 had majority foreign capital with authorization to operate as subsidiaries of foreign financial institutions, at the same time that 8 showed majority foreign capital while belonging to a financial group. Figure 3.1 shows the structure of the market in 2011 and previous years.

**Figure 3.1** Market structure of the insurance sector from 2001 to 2011



Source: Recovered from (CNSF, 2011)

## 2). Growth

At year end 2011, the CNSF (2011) reported that total emitted premiums for the insurance sector was 281, 792.1 million pesos, with this amount providing 3.9% of GDP. This amount represents real growth of 9.8% over the previous year.

c) Composition of portfolio: The portfolio composition at the end of 2011 according to the CNSF (2011) is as follows: Life, 39.6% Automobile 20.3%; Accidents and diseases, 15.1%; Fire and earthquake, 9.8%, Pension, 5.7% Miscellaneous, 3.8 %, Maritime and transport, Social responsibility, 2.1% and other sectors, 1.1%.

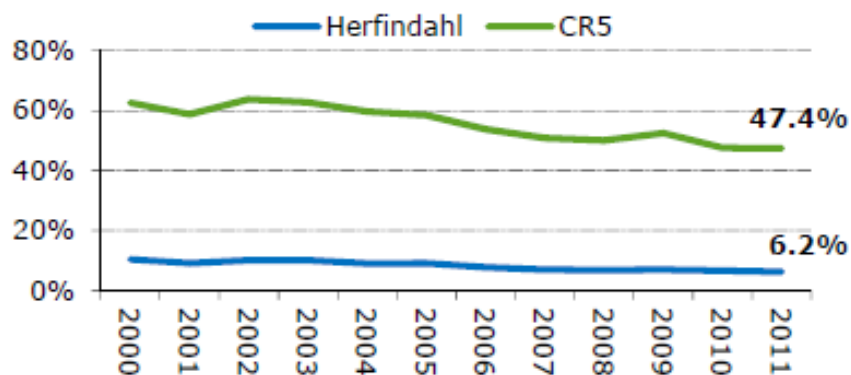
Insurance companies are characterized by either the asset or investment risk, although insurance regulations require holding larger amounts of financial securities (IMF 2002, p. 33). Insurance companies may have an “underwriting risk,” from their liabilities to be unable to pay their contractual obligations to policyholders due to miscalculations and low estimates of payouts relative to the premium charges, thus the inadequate technical provisions may not allow meeting the claims of policyholders. Insurance companies hold marketable instruments with long term contractual obligations giving insurance regulators more time to deal with financial distress and preventing “technical insolvencies caused by temporarily depressed market prices” (Troxel and Bouchie 1995, p. 8).

Contrary to the conclusions drawn by Herring and Schuermann, (2003), failures of insurance companies disrupt insurance market imposing private costs and may generate significant spillover impacts and contagions on other institutions and markets, as it was shown in the latest global financial crisis causing significant volatility in global capital markets.

#### d) Concentration and contribution to company growth

Insurance companies tend to form financial strategic alliances and conglomerates by having increasingly affiliated with other security firms and commercial banks. However, financial conglomerates containing banking and insurance companies raise questions of contagions within the group liabilities becoming vulnerable to confidence and demands of creditors. In 2011 the CNSF (2011) notes that concentrations decreased. CR5 index is obtained as the sum of the 5 largest holdings dial, the same largest market shares stood at 47.4%, 0.1 pp less than the previous year. Similarly, the Herfindahl index declined 6.5% to end 2010 at 6.2% at the end of 2011 (see Figure 3.2).

**Figure 3.2** CR5 and the Herfindahl index in the insurance industry of 2001-2011

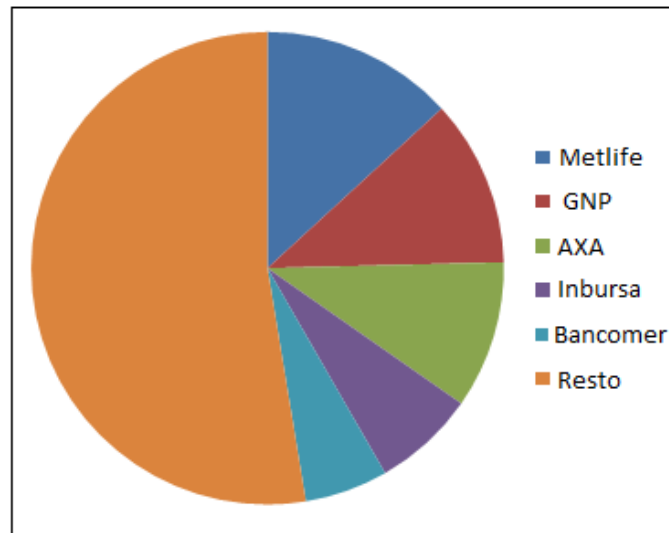


Source: Recovered from (CNSF, 2011)



Participation are settle down for the following companies: Metlife Mexico, S. A., 13.2%, Grupo Nacional Provincial, S. A. B., 11.4%, AXA Insurance, S. A. C. V, 10.1%; Insurance Inbursa, S. A., Grupo Financiero Inbursa, 7% and Seguros BBVA Bancomer, S. A. S. V., Grupo Financiero BBVA Bancomer, 5.7%. This is expressed graphically in Figure 3.3.

**Figure 3.3** Percentage of participation of the five leading companies in 2011



Source: Own elaboration with data from (CNSF, 2011)

#### e). Retrospective

When performing a retrospective analysis based on CNSF reports from December 2001 until December 2011, with regard to figures for the number of institutions, premiums written, the CR5, the Herfindahl index, clearly, this has been a growing market according to the number of competitors and sales (Table 3.1). Furthermore, we note that the CR5 and the Herfindahl index has been decreased year after year, pointing to a less oligopolistic market and more competition (Table 3.1).

**Table 3.1** Growth and concentration of the insurance sector from 2001 to 2011

Year	Number of firms	Emitted premiums (m of pesos)	Real Growth (%)	GDP (%)	CR5	Herfindahl index
2001	70	109,337	12.7	1.8	58.8	9
2002	81	128,883.5	12.1	2	62.3	9.7
2003	85	120,256.9	-9	1.3	62.8	10.1
2004	87	140,771	10.7	1.9	59.7	9
2005	86	140,886	-2.1	3	58.5	9.1
2006	91	166,240.5	13.5	4.8	53.8	7.7
2007	95	193,603	12.1	3.2	50.9	6.9
2008	100	209,994.6	1	1.3	50.1	6.8
2009	100	236,859.8	15.9	-8.2	57	8
2010	99	245,859.4	-9	5.5	47.6	6.9
2011	102	281,792.1	9.8	3.9	47.4	6.2

Source: Own elaborations with data from CNSF 2001-2011

Finally, in Table 3.2 it is reviewed the 5 companies in each year that were part of CR5 from 2001 to 2011. As can be seen, over this period, 2001-2011, only 11 different companies have been part of CR5 which reinforces the claim that it is an oligopolistic market, yet lose strength as demonstrated by the concentration indices (See table 3.2).

**Table 3.2** Companies that occupied the CR5 for the years from 2001 to 2011

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Comercial América	19	19.3	15.7	15.4	13.5						
GNP	16	15.3	16.2	16.8	18.4	15.1	13	12.2	10.2	11.4	11.4
Seguros Inbursa	9.1	12.6	6.8	6.5	6.1	5.6	6.8	5.4	17.4		7
Asegurador a Hidalgo	11.1	11.3									
Seguros Génesis	3.6	3.8									
Metlife México			19.1	15.2	15.7	14.9	14.2	14.5	13.7	15.3	13.2
Seguros Monterrey			5		4.8					5.1	
Seguros Banamex				5.8							
Seguros ING						12.2	11				
Seguros BBVA Ban.						6	5.9	6.7	7.5	5.2	5.7
AXA Seguros								11.3	8.2	10.6	10.1
<b>Total</b>	<b>58.8</b>	<b>62.3</b>	<b>62.8</b>	<b>59.7</b>	<b>58.5</b>	<b>53.8</b>	<b>50.9</b>	<b>50.1</b>	<b>57</b>	<b>47.6</b>	<b>47.4</b>

Source: Own elaboration with data from the CNSF 2001-2011

### **3.6 Research methods**

As mentioned earlier the purpose of this research is to analyze how strategic alliances have impacted the insurance industry in Mexico. In general, it is described the strategic alliances in the entire sector according to the information collected. In particular, they are explored the five companies that formed the CR5 at year end 2011 (see Figure 3.3).

### **3.7 Results**

Here are the alliances and acquisitions that have made these five companies related to the three theories discussed in this research.

#### **3.7.1 Resource-based theory**

The main resource for an insurance company is capital. In the insurance sector at the end of 2011, 57 companies are subsidiaries of foreign companies and 15 belong to financial groups. Therefore, through these agreements are obtained the capital necessary to operate in that sector. With respect to the five leading companies (MetLife, 2012) and AXA (AXA, 2012) are foreign subsidiaries, GNP (GNP, 2012) belongs to a corporation (Grupo BAL), Insurance Inbursa (Inbursa, 2012) and Seguros BBVA Bancomer (Bancomer, 2012) belong to financial groups.

It can therefore conclude that the success of these five companies is partly due to these agreements for access to more capital.

#### **3.7.2 Theory based on the industry**

The insurance sector consists of several branches as seen in the composition of the portfolio. Many insurer companies are groups of firms that together in collaboration span the entire portfolio of the sector (Life insurance, automobile accidents and diseases, fire and earthquake, pensions, miscellaneous, maritime and transport, social responsibility, and other classes, and thus compete against other groups within the market. Regarding the five leading companies, Metlife (Metlife, 2012) and AXA (AXA, 2012) are foreign subsidiaries. GNP (GNP, 2012) belongs to the corporation Grupo BAL. Together these companies compete in the insurance sector covering all the needs. Seguros Inbursa (Inbursa, 2012) and Seguros Bancomer (Bancomer, 2012) and Seguros BBVA Bancomer (Bancomer, 2012) belong to financial groups. Therefore, it can be concluded that the success of this five companies in part is due to the agreements to have access to large pools of capital.

### 3.7.3 Theory based on institutions

The great growth experienced by the insurance industry in Mexico is due to the free entry of foreign direct investment (FDI) after 1994 and North America free Trade Agreement (NAFTA). This can be observed by the large number of subsidiaries that are competing in the Mexican insurance market. In addition, MetLife and AXA decided to operate as businesses traditionally made by means of which arrived in Mexico, such as Insurance Hidalgo and Seguros Génesis which are the Insurance companies acquired by MetLife (MetLife, 2012). ING Insurance was acquired by AXA (AXA, 2012) and then incorporates their multinational philosophies. This leads to conclude that they decided to learn from the Mexican market through these companies to enter fully later.

### 3.8 Discussion and conclusions

The numbers suggest that the alliances, mergers and acquisitions are crucial and dominate the insurance sector. Through these, the companies compete, grow and explore new markets. It has been shown that alliances, mergers and acquisitions are present in the five leading insurance companies in the sector at the end of 2011. This leads to conclude that they are source of competitiveness, growth and expansion. The three theories presented were consistent with what is reflected in the insurance sector. However, further studies can be performed according to each one of them. For example, one issue is the access to tangible resources such as capital through strategic alliances. It is needed to be answered if there is also access to intangible resources and the experience and knowledge in the insurance sector. As this question, many other questions arise from this research.

### 3.9 References

- Asociación Mexicana de Instituciones de Seguros A.C. Sector Seguros (1991). *Posición del sector seguros ante las negociaciones del Tratado de Libre Comercio*. México: AMIS.
- AXA. (2012). AXA. Recuperado el 28 de Mayo de 2012, de <http://www.axa.mx>
- Bancomer. (2012). *Seguros BBVA Bancomer*. Recuperado el 28 de Mayo de 2012, de <http://www.segurosbancomer.com.mx>
- Barney, J. (1991). "Firm Resources and Sustained Competitive Advantage". *Journal of Management*. 17 (1): 99-120.
- Barney, J. (1986). "Strategic Factor Market: Expectations, Luck, and Business Strategy". *Management Science*. 32 (10): 1231-1241.

CNSF. (2011). *Comisión Nacional de Seguros y Fianzas*. Recuperado el 28 de Mayo de 2012, de <http://www.cnsf.org.mx>

Eisenhardt, K. and Schoonhoven, C. (1996). "Resource-Based View of Strategic Alliance Formation: Strategic and Social Effects in Entrepreneurial Firms". *Organization Science*, 7, 136-150.

Das, T. K. and Teng, B. (2002). "Alliance Constellations: A Social Exchange Perspective". *Academy of Management Review*, 27(3): 445-456.

Gulati, R. (1998). "Alliances and Networks". *Strategic Management Journal*, 19: 293-317.

Gulati, R., Nohria, N. and Zaheer, A. (2000). "Strategic Networks". *Strategic Management Journal*, 21:203-215.

GNP. (2012). *Grupo Nacional Provincial*. Recuperado el 28 de Mayo de 2012, de <http://www.gnp.com.mx>

Grant, R and Baden-Fuller, C (2004) "A Knowledge Accessing Theory of Strategic Alliances," *Journal of Management Studies*, 41(1): 61-84.

Herring, R., Schuermann, T. (2003). "Capital Regulation for Position Risk in Banks, Securities Firms and Insurance Companies" in H. Scott (ed.) *Capital Adequacy: Law, Regulation, and Implementation*, Oxford.

IMF. (2002). *Global Financial Stability Report: A Quarterly Report on Market Developments and Issues*. A Report by the International Capital Markets. Department on Market Developments and Issues. International Monetary Fund.

Inbursa. (2012). *Seguros Inbursa*. Recuperado el 28 de Mayo de 2012, de <http://www.inbursa.com>

Laurell, A. C. (1994). La salud: de derecho social a mercancía. In: *Nuevas Tendencias y Alternativas en el Sector Salud* (A. C. Laurell, org.). México: Universidad Autónoma de México.

Metlife. (2012). *Metlife México*. Recuperado el 28 de Mayo de 2012, de <http://www.metlife.com.mx>

Peng, M. W. (2007). *Estrategia Global*. México D. F.: CENGAGE Learning.

Porter, M. (1980). *Competitive Strategic: techniques for analyzing industries and competitors*, Free Press, New York.

Ruíz-Ramírez, T. (1992). *La Industria del Seguro ante la Integración Económica*. México, 13 de mayo (Mimeo.).

Tamez, S.; Bodek, C. & Eibenschutz, C. (1995). *Public and Private: Insurance Companies and Medical Care in Mexico*. Cad. Saúde Públ., Rio de Janeiro, 11 (4): 579-587, Oct/Dec, 1995.

Troxel, T. E., and Bouchie, G. E. (1995). *Property-Liability Insurance Accounting and Finance*, 4th edition. Malvern: American Institute for CPCU.

Wernerfelt, B. (1984) . “A Resource-based View of the Firm”. *Strategic Management Journal*, 5: 171-180.

Zervos, S. (2004) “The Transactions Costs of Primary Market Issuance: The Case of Brazil, Chile, and Mexico”. *World Bank Policy Research Working Paper 3424*, October 2004.