



## TAKAFUL INSURANCE COMPANIES' CLAIM PAYMENT AND GROWTH OF SMEs IN NIGERIA

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### **Abstract**

*The establishment of a thriving Takaful insurance subsector of the Nigerian insurance go a long way in driving entrepreneurship in the Northern Nigeria especially among the Moslems who might have reservations for the use of conventional insurance for the protection of their risks and those of their business; and also, for them to benefit from other financial intermediation accruing from the insurance industry. The non-purchase of the Takaful insurance products by these SMEs could be as a result of the non-affordability of the premiums to be paid by the SMEs owners, the fear of non-payment of claim after the insured event could have happened. The survey method was adopted in carrying out this research. This entails the use of questionnaire and interviews to triangulate and justify the impact of Takaful insurance on the development of small and medium enterprises in the country. The simple random sampling method was applied. Thus, the 487 respondents would be picked randomly from the owner/managers of SMEs who insure these Takaful insurance companies. With a coefficient of 0.318 and a low standard error (0.036), TCS has a substantial positive impact on business performance. The multiple regression results underscore the positive and significant impacts of Takaful premium affordability, claims settlement, Islamic principles, risk management consultancy support, customer service, and education and awareness initiatives on SMEs' overall performance. These findings emphasize the importance of embracing Takaful principles and services as integral elements for enhancing the financial and operational aspects of SMEs.*

**Keywords:** Insurance, Claims payment, Takaful, Final payment, Risk Management

### **Introduction**

The establishment of a thriving Takaful insurance subsector of the Nigerian insurance go a long way in driving entrepreneurship in the Northern Nigeria especially among the Moslems who might have reservations for the use of conventional insurance for the protection of their risks and those of their business; and also for them to benefit from other financial intermediation accruing from the insurance industry. It is pertinent to note that existing studies have primarily focused on the impact of either conventional insurance and micro insurance policies on the performance of SMEs and these studies have concentrated in the Southern Nigerian mainly with little or none of such studies on the experiences from the Northern part of the country. Moreover, the majority of these studies on insurance have not taken time to examine the adoption of Takaful insurance with regard to Nigeria which is predominantly an Islamic region and how it could help the SMEs owners protect their businesses and derived the added advantages of using insurance as a risk protection mechanism (Abdul-Malig & Salauden, 2015, and Ardo, 2017).



The non-purchase of the Takaful insurance products by these SMEs could be as a result of the non-affordability of the premiums to be paid by the SMEs owners, the fear of non-payment of claim after the insured event could have happened. It could be that some of these SMEs owners might still not believe that the insurance model aligns with Islamic principles, or that the Takaful insurance companies are not providing adequate risk management consultancy services to the SMEs. The customer services from the Takaful insurance companies may not meet the requirements of the SMEs owners and such they prefer to carry their risks by themselves. Lack of awareness of education of the benefits derivable from the use of Takaful insurance as a model for risks protection could be the reasons for the low patronage and finally it could be as a result of low technology integration by the Takaful insurance companies. All these could have negative effect on risks protections by the SMEs owner in Nigeria and thereby effecting the performances of these business on the long run. The aim of this study is to examine the impact of Takaful claims settlement on business performance of Small and Medium Enterprises in Nigeria.

## Literature Review

### General Overview of Takaful Insurance

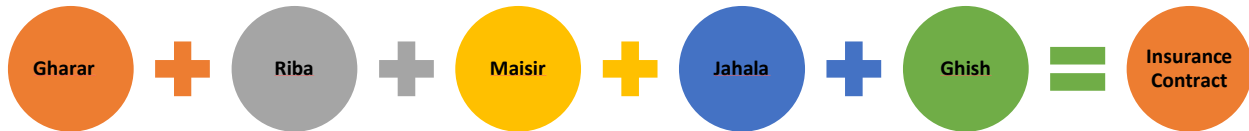
The term Takaful according Alhabshi & Razak (2022) has an Arabic root of *kafala* which means to guarantee and in terms of usage and implication, the term *kafala* denotes the agreement by one party to indemnify another for liability that had been agreed earlier on. Alhabshi & Razak posited that Takaful has proven to be the fastest growing sector of the insurance market with unprecedented double-digit rate of sustainable growth over the years. It is with this mind that Abubakar, Ogunbado & Saidi (2017) describe Takaful as the Islamic alternative to insurance of the conventional system, which they termed as an efficiently applied systems of cooperative risk sharing. However, Abubakar, *et al* (2017) argued that Takaful is not different in its philosophy with conventional insurance as it is an *idea* that focuses on mutual cooperation between members in order to secure their mutual protection. This brand of insurance has been used in most countries to grow their insurance penetrations. Islamic insurance also known as Takaful, is an alternative model to conventional insurance; which is forbidden in Islam, it having some elements which are against Islamic law such as *riba* (usury), *gharar* (ambiguity), and *maisir* (gambling) (Shafique, *et al* 2015). In contrast to conventional insurance, Takaful, according to Shafique, *et al* (2015) is incorporated on the base of mutual assistance, responsibility, mutual protection and assurance, which is incorporated into the concept of *tabarru* (donation). The operation of Takaful model is shown in the figure 2.7 below.

Most Moslems began to avoid instruments which they believed as being non Shariah compliant including insurance products that they had seen as a form of gambling.

This should not be the case with insurance as both the conventional insurance and Takaful have a lot of similar elements. This might be the reason for Dahnoun and Alqudwa to further argue that both Takaful and conventional insurance policies work on the same basic system, which is the pooling of funds to manage the risk of a group of people. Having said that, there are major differences in the workings of the two systems, stemming from the fact that Takaful adheres strictly to the Islamic principles which it was developed upon. However, they noted that while the conventional investment units of insurance invest based on their assessment of what fits their profiles, Takaful investments follow strict Shariah based principles. They cannot invest in anything containing elements of gambling, uncertainty and usury (practice of lending money at unreasonably high interest rates). This is regulated by Shariah requirements specified by the

regulator. Muslim scholars have declared conventional insurance as haram (prohibited) (Dahnoun & Alqudwa, 2018). This position is depicted in the figure 2.8 below.

**Figure 2.8: Contents of conventional insurance which makes it non-Shariah compliant**



Source: Yusof, M.F., Ismail, U.Z.W & Naqim, A.K. M.N. (2015) Takaful: Operations and Business Competence, p. 160.

Human beings according to Nazarov & Dhiraj (2019) are naturally inclined towards safeguarding and protecting themselves from future misfortunes, which may fall within the realms of risk mitigation, a concept that gave birth to insurance. At this juncture, it is important to observe that insurance is a mutual agreement between two parties to protect one of them from unexpected future financial loss (Hussain, 2011). This is the reason that Pfefer (1956, p.53) defined insurance from the conventional perspective as “a device for the reduction of risk of one party, called the insured, through the transfer of particular risks to another party, called the insurer, who offers a restoration, at least in part, of economic losses suffered by the insured”. The major difference between using insurance or Takaful products and conventional insurance lies more on that the later does not comply with the provisions of Shari’ah. To this end, Salman, *et al* (2015) noted that when the insurance companies receive the premium from the policyholders, they normally use them to generate income to pay claims and pay dividends to the shareholders. The need to generate more funds in this regard normally makes them to invest in securities which are not Sharia’h compliant from which they might earn interest. Referring to insurance as a game, Salman, *et al* (2015) stated that the policyholders will win if they make claims but if not, they will lose the premium; while the insurer will gain if the policyholders do not make any claim but if they do, the insurer will become the loser. In other words, this practice could be seen as a form of gambling they had argued. The end result, according to Salman, *et al* (2015) is that it will bring injustice to the society; since gambling in insurance is a form of uncertainty. More so, that the future could from this perspective to be seen as uncertain and policyholders are unsure where particular unfortunate event will hit them. In this way, conventional insurance is prohibited in Islam due to the involvement of prohibited elements such as interest, uncertainty, and gambling (Salman, *et al*, 2015).

### **The Concept of development/growth of small and medium enterprises**

SME stands for Small and medium-sized enterprises (SMEs) or small and medium-sized businesses (SMBs) are business whose personnel numbers fall below certain limits (Al-Herwi, 2019). Al- Herwi (2019) posited that the SME sector plays an extremely important part in modern economy, proving to be the most attractive and tremendous innovative system. The number of employees in SMEs vary from industry to industry. According to Njanike, K. (2019) the appropriate involvement of Small and Medium Enterprises (SMEs) in industrial activities globally is an incontestable truth. This shows that small and medium sized enterprises are very important in an economic and for economic development.



Mills, Reynolds & Herculano (2022) revealed that small and medium-sized enterprises (SMEs) are the foundation of the global economy, representing 90% of all businesses and accounting for nearly 70% of global jobs and GDP. In the same vein, International Finance Corporation (2022) had observed that these businesses power the supply and distribution chains of key industries. That is that SMEs play a central role in society, helping to strengthen economic inclusion, supplying goods and services to poor and underserved markets and providing employment to many women entrepreneurs (Mills, Reynolds, & Herculano, 2022; International Labour Organisation, 2019). These companies, according to European Investment Bank Group (2022), are also key drivers of innovation, offering fresh ideas and new products, being able to adopt change more quickly than large companies and having high growth potential.

Small-medium enterprise (SME) formation and venture start-ups, according to Adeosun & Shittu (2012) always create excitement for economists, politicians, unemployed youths and consumers alike. There is an overcoming inertia to move from idea conceptualisation to actual implementation in a tough clime like Nigeria or Sub Sahara Africa; in Nigeria is a daunting task (Anyebe, 2017). On the global ease of doing business report, Nigeria has always fared badly, ranking 146 in 2019 and 131 in 2020 (World Bank, 2020) with only marginal improvement in recent years. The experience in the global innovation index While many informal SMEs abound and further undermine registered SMEs as they operate at a lower cost due to tax evasion and other levies (Aribaba et al., 2019), it is important to evaluate the formation of SMEs and economic growth in Nigeria.

Otaru (2022) quoting a report jointly released by the Small and Medium Enterprises Development Agency of Nigeria (SMEDAN) and the National Bureau of Statistics (NBS) in Abuja stated that there are over 39.65m MSMEs operating in Nigeria and a breakdown of the figures showed that micro enterprises (MEs) accounted for 38,413,420 million, while the total number of small and medium enterprises (SMEs) stood at 1,240,965 million representing 3.1 per cent. Oturu (2022) also cited the report as stating that MSMEs in Nigeria contributed 46.31 percent to the country's gross domestic product (GDP) and accounted for 96.7 per cent of businesses. This shows the importance of SMEs in the Nigerian economy and how they contribute to economic growth of the country.

## **Research Methods**

The survey method was adopted in carrying out this research. This entails the use of questionnaire and interviews to triangulate and justify the impact of Takaful insurance on the development of small and medium enterprises in the country. The survey research design was adopted for this study and a cross sectional questionnaire was used to collect data from the field from the target respondents. The target population for the study was derived from the clients of the two prominent Takaful insurance companies in Nigeria using their database. This is a quantitative research whereby statistical sampling method was used for the collection of data from respondents from the two companies.

The random sampling technique is used for the collection of data for the study. The reason for the adoption of this method is to ensure that all the characteristics of the population (especially with regards to the sizes of the companies are reflected in the sample). The simple random sampling method was applied. Thus, the 487 respondents would be picked randomly from the owner/managers of SMEs who insure these Takaful insurance companies.



**Data Analysis and Results**

This section provides an in-depth exploration of the multiple regression analysis, shedding light on the intricate web of relationships and predictive qualities within the variables. Regression analysis shows the effect of independent variables on the dependent variables. This study examined the effect of Takaful insurance and performance of small and medium enterprises in Nigeria. The seven dimensions of Takaful insurance which is the independent variable are Takaful premium affordability, Takaful claims settlement, Takaful Islamic principles, Takaful risk management consultancy support, Takaful customer service and support, Takaful education and awareness initiatives and Takaful technology integration. The table 1, Table 2 and Table 3 below show the results of the regression analysis between the independent and dependent variable.

**Table 1: Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.663 <sup>a</sup>	.439	.429	.33917

a. Predictors: (Constant), TTI, TIP, TCSS, TRMC, TEAI, TPA, TCS

**Note:** TCSS = Takaful Customer Service and Support, TEAI = Takaful Education and Awareness Initiatives, TCS = Takaful Claims Settlement, TIP = Takaful Islamic Principles, TRMC = Takaful Risk Management Consultancy Support, TPA = Takaful Premium Affordability, TTI = Takaful Technology Integration, BUSP = Business Performance

Table 1 presents the model summary for the multiple regression analysis, offering an overview of the predictive power and goodness-of-fit of the model. The coefficient of determination (R-squared) is 0.439, indicating that approximately 43.9% of the variance in Business Performance can be explained by the included predictors—Takaful Technology Integration (TTI), Takaful Islamic Principles (TIP), Takaful Customer Service and Support (TCSS), Takaful Risk Management Consultancy Support (TRMC), Takaful Education and Awareness Initiatives (TEAI), Takaful Premium Affordability (TPA), and Takaful Claims Settlement (TCS). The adjusted R-squared, which considers the number of predictors in the model, is 0.429. The standard error of the estimate is 0.33917, representing the average distance between the observed and predicted values.

**Table 2: ANOVA<sup>a</sup>**

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	34.296	7	4.899	42.590	.000 <sup>b</sup>
	Residual	43.829	381	.115		
	Total	78.125	388			

a. Dependent Variable: Business Performance

b. Predictors: (Constant), TTI, TIP, TCSS, TRMC, TEAI, TPA, TCS

**Note:** TCSS = Takaful Customer Service and Support, TEAI = Takaful Education and Awareness Initiatives, TCS = Takaful Claims Settlement, TIP = Takaful Islamic Principles, TRMC = Takaful Risk Management Consultancy Support, TPA = Takaful Premium Affordability, TTI = Takaful Technology Integration.



Moving to Table 2, the ANOVA results indicate the overall statistical significance of the regression model. The F-statistic is 42.590, with a corresponding p-value of 0.000. This suggests that at least one of the predictors significantly contributes to explaining the variance in Business Performance. The regression model is statistically significant, providing evidence that the combined effect of the predictors is not due to chance.

**Table 3: Coefficients<sup>a</sup>**

Model		Unstandardized Coefficients		Standardized	T	Sig.
		B	Std. Error	Coefficients		
1	(Constant)	.073	.300		.243	.808
	TPA	.093	.041	.091	2.265	.024
	TCS	.318	.036	.377	8.760	.000
	TIP	.117	.030	.152	3.907	.000
	TRMC	.098	.042	.091	2.315	.021
	TCSS	.175	.042	.163	4.146	.000
	TEAI	.189	.037	.217	5.112	.000
	TTI	.070	.039	.070	1.774	.077

a. Dependent Variable: Business Performance

**Note:** TCSS = Takaful Customer Service and Support, TEAI = Takaful Education and Awareness Initiatives, TCS = Takaful Claims Settlement, TIP = Takaful Islamic Principles, TRMC = Takaful Risk Management Consultancy Support, TPA = Takaful Premium Affordability, TTI = Takaful Technology Integration.

In Table 3, the constant term represents the estimated value of the dependent variable when all predictors are zero. In this case, the constant is 0.073, but it is not statistically significant ( $p = 0.808$ ). This value is interpreted as the baseline or starting point for business performance, but its non-significance suggests that business performance is significantly influenced by the included predictors.

### Discussion of Results

Second, the multiple regression result indicated that Takaful claims settlement has a positive and significant effect on business performance of Small and Medium Enterprises in Nigeria. The positive and significant effect of Takaful claims settlement on the business performance of Small and Medium Enterprises (SMEs) in Nigeria is justified by the pivotal role of efficient claims resolution in bolstering SMEs' financial stability and operational continuity. Timely and effective claims settlement ensures that SMEs can recover swiftly from unforeseen losses or disruptions, reducing financial strain and enhancing their ability to navigate challenges. This positive impact fosters a sense of security and confidence among SMEs, encouraging them to invest in Takaful coverage. As a result, SMEs experience improved risk management, reduced financial uncertainties, and ultimately, heightened business performance. The findings underscore the critical importance of Takaful claims settlement in fortifying the resilience and success of SMEs in the dynamic business landscape of Nigeria.

The positive and significant impact of Takaful claims settlement on the business performance of Small and Medium Enterprises (SMEs) in Nigeria is supported by empirical



studies exploring related aspects of claims settlement and its consequences in different contexts. Ayuba et al. (2020) investigate the influence of claims settlement on the performance of general insurance businesses in Nigeria and find a significant positive impact on the selected insurance companies. Similarly, Hagos (2019) explores the effect of claim settlement service quality on repurchase intention in Ethiopian insurance companies, emphasizing the importance of effective claims handling to maintain customer loyalty. Oyetunji et al. (2021) examine the relationship between poor claims settlement and the demand for insurance policies in Nigeria, affirming a significant negative effect on policy demand. Together, these studies provide a consistent foundation for the notion that effective and timely claims settlement positively influences the overall performance and customer relations of insurance businesses, aligning with the findings from the study.

Takaful Claims Settlement (TCS): With a coefficient of 0.318 and a low standard error (0.036), TCS has a substantial positive impact on business performance. A one-unit increase in TCS is associated with a 0.318 increase in business performance. This effect is highly statistically significant ( $p = 0.000$ ), emphasizing the importance of efficient claims settlement in enhancing overall business performance.

### **Conclusion**

In conclusion, this study sheds light on the vital role of Takaful components in influencing the business performance of Small and Medium Enterprises (SMEs) in Nigeria. The multiple regression results underscore the positive and significant impacts of Takaful premium affordability, claims settlement, Islamic principles, risk management consultancy support, customer service, and education and awareness initiatives on SMEs' overall performance. These findings emphasize the importance of embracing Takaful principles and services as integral elements for enhancing the financial and operational aspects of SMEs.

### **Recommendations**

This study found that Takaful claims settlement has a positive and significant effect on business performance of Small and Medium Enterprises in Nigeria. Therefore, this study recommended that financial institutions should prioritize partnerships with Takaful providers known for efficient claims settlement. Collaborating with reputable Takaful entities can enhance the overall risk management strategy of institutions, fostering trust and reliability in business operations. Similarly, Takaful industry players must continue to streamline and improve their claims settlement processes. Investing in advanced technologies and transparent communication channels will bolster the industry's credibility and attractiveness to Small and Medium Enterprises, ensuring prompt and fair claims resolutions. Also, regulatory bodies should monitor and enforce standards for timely claims settlement within the Takaful sector. Regular audits and stringent oversight will maintain industry integrity, protecting the interests of businesses relying on Takaful services. The government should support initiatives that promote fair and expeditious claims settlements. Incentivizing Takaful companies to uphold high standards in this regard contributes to economic stability and reinforces confidence in the broader business ecosystem.



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