The impact of the establishment of a captive insurance company on the risk characteristics of its parent company

Chih-Wei Chao 1, *
Wen-Yi Lin 2
Y. Angela Liu 1

1 Department of Business Administration
National Chung Cheng University
No. 168, University Rd
Minxiong, Chia Yi 621
Taiwan, R.O.C.

2 Department of Economics and Law
Feng Chia University
No. 100, Wenhwa Rd.
Taichung 407
Taiwan, R.O.C.

Abstract
Whether the establishment of captive insurance company can effectively alter the parent company’s risk characteristics is an issue of academic as well as practical importance, and thus has attracted wide research interests. Specifically, the extent of literature has proposed various hypotheses concerning the impact of captive insurance company on the systematic and unsystematic risks of its parent company. This paper employs data of captive insurance company that were established in the U.S. between 1960 and 2007, and further examines the change, if any, of parent company’s risk characteristics after the establishment of captive insurance company. Using matched pairs of firms with and without captive insurance company, our findings show that neither the systematic risk nor the unsystematic risk of the parent company is significantly altered due to the establishment of captive insurance company, suggesting such action provides no additional risk reduction or diversification benefit to the parent firm.

Keywords and phrases: Captive insurance company, systematic risk, unsystematic risk.

*E-mail: dbawaynechao@yahoo.com.tw

Journal of Interdisciplinary Mathematics
Vol. 13 (2010), No. 4, pp. 475–490
© Taru Publications