Life Insurance Sector in India: Opportunities and Challenges

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Abstract

Indian economy and industry has undergone significant transformation since 1991 moving away from state controlled to a competitive market economy. The most remarkable of this transformation has been noted in the financial sector, particularly, in the Indian Insurance Industry which has opened up to all competitors, integrating financial services to the global economy. IRDA was established in 1999 to protect the interest of policyholders for promoting and ensuring orderly growth of the insurance industry. Indian Insurance Company means, any insurer being a company which is formed and registered under the companies Act, 1956. FDI cannot be viewed from the financial perspective alone. It brings experience sharing, technology up-gradation, specialized skills, better operational efficiency, improved perceptions by reinsurance companies, and faster evolution of industry. Since Indian Insurance market is getting integrated into Global Insurance Industry, we must analyse and understand opportunities and challenges of Insurance business in India.

***Keywords**: Life Insurance, Products Offered, Challenges, Opportunities.*

Introduction

The insurance sector in India has grown at faster rate after liberalization. Life Insurance is one of the fastest growing and emerging markets in India. Insurance penetration in the country is low mainly in rural area. The Insurance Industry has a significance contribution in socio-economic development. A majority of the underprivileged & rural poor society is still not insured and untouched by the benefits of Life Insurance. There is a tremendous scope for developing insurance business in the rural areas where human life and income generating rural assets need more protection. IRDA has acknowledged various reforms and initiatives for the welfare of rural people i.e. Micro-insurance especially designed to provide life insurance benefit to rural and economically backward class of the society. Insurance companies have a pivotal role in offering insurance products which meet the requirements of the people and, at the same time, are affordable. Some of the challenges faced by the insurance sector pertain to the demand conditions, competition in the sector, product innovations, delivery and distribution systems, use of technology, and regulation.

Current State of the Life Insurance Sector

The life insurance industry has witnessed a phenomenal increase in demand over the last few years. The main reason for this change is the growing awareness about the importance of life insurance, increasing life expectancy rates, changing demographics, etc. a large number of private sector players have entered this market as customers now

demand highly customized products and prompt service. The life insurance industry in India was nationalized under the Life Insurance Corporation Act of 1956. Until 1999, when the Insurance Regulatory and Development Authority Act were passed, LIC was the only life insurance provider. Since liberalization, a total of 24 life insurance companies have been formed, with the majority of them being joint ventures with foreign companies.

Globally, the share of life insurance business in total premium was 56.2 per cent. However, the share of life insurance business for India was very high at 79.6 per cent while the share of non-life insurance business was small at 20.4 per cent. In life insurance business, India is ranked 11th among the 88 countries, for which data is published by Swiss Re. India's share in global life insurance market was 2.00 per cent during 2013. However, during 2013, the life insurance premium in India declined by 0.5 per cent (inflation adjusted) when global life insurance premium increased by 0.7 per cent. At the end of September 2014, there are 53 insurance companies operating in India; of which 24 are in the life insurance business and 28 are in non-life insurance business. In addition, GIC is the sole national reinsurer. Of the 53 companies presently in operation, eight are in the public sector - two are specialized insurers, namely ECGC and AIC, one in life insurance namely LIC, four in non-life insurance and one in reinsurance. The remaining forty five companies are in the private sector (Table -1).

Table -1: Registered Insurers in India (As on 30th September, 2014)

Type of business	Public Sector	Private Sector	Total
Life Insurance	1	23	24
Non-life Insurance	6*	22**	28
Reinsurance	1	0	1
Total	**8**	**45**	**53**

* Includes Specialised insurance companies - ECGC and AIC.

** Includes five Standalone Health Insurance Companies – Star Health & Allied Insurance Co., Apollo Munich Health Insurance Co., Max Bupa Health Insurance Co., Religare Health Insurance Co., and Cigna TTK Health Insurance Co. Source: *Annual Report, IRDA, 2013-14.*

Life insurance industry recorded a premium income of Rs. 3,14,283 crore during 2013-14 as against Rs. 2,87,202 crore in the previous financial year, registering a growth of 9.43 per cent (0.05 per cent growth in previous year). While private sector insurers posted 1.35 per cent decline (6.87 per cent decline in previous year) in their premium income, LIC recorded 13.48 per cent growth (2.92 per cent growth in previous year). On the basis of total premium income, the market share of LIC increased from 72.70 per cent in 2012-13 to 75.39 per cent in 2013-14. Accordingly, the market share of private insurers has declined from 27.30 per cent in 2012-13 to 24.61 per cent in 2013-14 (Table 2).

Table 2: Premium Underwritten & Market Share: Life Insurers (Rs. in Crore)

Year	2012-13			2013-14		
Insurers	LIC	Private Sector	Total	LIC	Private Sector	Total
1. Regular premium	30,313.52 (-24.58) (58.13)*	21,834.53 (-0.94) (41.87)*	52,148.05 (-16.21) (100)*	31,904.49 (5.25) (60.56)*	20,780.83 (-4.83) (39.44)*	52,685.32 (1.03) (100)*
2. Single premium	46,297.98 (11.11) (83.85)*	8,915.05 (-11.20) (16.15)*	55,213.03 (6.78) (100)*	58,904.30 (27.23) (87.09)*	8,730.05 (-2.08) (12.91)*	67,634.35 (22.50) (100)*
3. First Year Premium (3 =1+2)	76,611.50 (-6.41) (71.36)*	30,749.58 (-4.15) (28.64)*	1,07,361.08 (-5.78) (100)*	90,808.79 (18.53) (75.47)*	29,510.88 (-4.03) (24.53)*	1,20,319.67 (12.07) (100)*
4. Renewal Premium	1,32,192.08 (9.23) (73.50)*	47,649.33 (-8.55) (26.50)*	1,79,841.41 (3.88) (100)*	1,46,133.51 (10.55) (75.34)*	47,830.02 (0.38) (24.66)*	1,93,963.53 (7.85) (100)*
5. Total Premium (5 =3+4)	2,08,803.58 (2.92) (72.70)*	78,398.91 (-6.87) (27.30)*	2,87,202.49 (0.05) (100)*	2,36,942.30 (13.48) (75.39)*	77,340.90 (-1.35) (24.61)*	3,14,283.20 (9.43) (100)*

Note: 1. Figures in brackets indicate the growth (in per cent) over the previous year. 2. Figures in * brackets indicate the market share (in per cent). Source: *Annual Report, IRDA, 2013-14.*

Products Offered

Life insurance products are offered either for individuals or groups.

Individual products:

1. ***Participating products:*** In participating policies, insurers are required to share any surplus generated with the policyholders. This includes Money Back, Endowment, Whole Life variants, etc. These policies are the most dominant product range in the middle income segment as they are a source of savings for customers, give assured returns, and cater to non-investment savvy consumers. However, these products are pooled investments and are often not adequately transparent with consumers.

2. ***Unit-linked (ULIP):*** These policies are becoming increasingly popular as they provide a combination of contingency coverage and market-linked investment returns. For most insurance companies, especially the new private sector ones, ULIPs account for approximately 90% of their total portfolio. ULIPs primarily cater to high income and/or investment-savvy clients. These products are generally more

flexible but have a higher risk associated with them. Capital requirement is lower, as compared to other policies, because most of the investment risk is borne by the policyholders.

3. ***Pure risk cover products:*** These products are the simplest form of insurance. They include term with return of premium variants. In the last few years, their popularity has increased as consumers purchase them with housing loans. However, their contribution to the sector as a whole is still small as people focus on savings and investment-type policies.

4. ***Riders:*** These are extra coverage policies that policyholders purchase to supplement their principal policies. They include accidental death and dismemberment, health and illness, pure term, and waiver of premium variants. Due to high costs and lack of trained agents, riders are not very common in India. However, these products are highly profitable.

Group products:

1. ***Group protection:*** These are yearly group term contracts, single premium, deposit-linked, loan/mortgage cover variants. Group products are primarily sold to employer-employee groups. In most cases, affinity group segments buy them. These products are highly price-sensitive and have a long gestation period for sales.

2. ***Group funds:*** These include super-annuation, gratuity funds, leave encashment variants, etc. These products are also highly price sensitive and have a long gestation period for sales. As the investment track record and servicing standards of a company are the key to its sales, specialized sales teams are required for such funds. These products have low profitability and high capital requirements to maintain solvency.

Innovative products

The growth in the number of insurance companies has reiterated the need for companies to differentiate themselves to increase their market share. Product innovation is one of the best tools for companies to increase their presence in the market by offering products that suit their customers best. The most significant product innovation to take place in the life insurance segment is the launch of ULIPs, which have become extremely popular due to their insurance-cum-investment profile. Higher returns amid a sustained bull run in equity markets have also contributed to their popularity. Both traditional and unit-linked products are positioned for various customer segments such as child, women, health, retirement, whole life, endowment, etc. Due to its inadequate penetration (only 10% of the working population is covered), the pension sector has tremendous potential for insurance companies to be more innovative.

Challenges

1. **Money laundering in insurance:** Mutual funds and banking products have traditionally been more susceptible to money laundering. Insurance has not been a favourite sector for money launderers because of its typical way of functioning whereby only a premium is charged upfront for the promise of a huge contingent payment later. But in the wake of innovations such as single premium policies and unit-linked plans, the insurance sector has become far more prone to money laundering than it was earlier. Companies characterized by large customer bases and their dependence on third parties for sourcing their businesses

are soft targets for money launderers as it makes it relatively easier for them to hide their dubious intentions. In this regard, Indian insurance companies have to deal with issues emerging from geographically dispersed distribution networks and contact points through the agency sales force. Apart from establishing comprehensive KYC norms, they would also have to put in place processes to know the agents.

2. **Solvency Norms:** Solvency is a part of prudential norms and as risks increase across markets, the solvency margin also needs to go up tangentially. In order to satisfy the solvency margin requirements, companies have to systematically build up reserves by transferring a part of the surplus to a special reserve called "Solvency Margin Reserve." However, transferring the surplus will result in a reduction in bonus rates declared and make insurance unattractive vis-a-vis other financial instruments. Therefore, only a part of the amount needed to meet solvency margin requirements can come from the surplus held back. The balance requirement has to be met by other sources for capital, which include:

- Share capital
- Free reserves in the shareholders' fund
- Difference between the market value and book value of assets

This coupled with the constraints on capital raising (FDI restrictions in private insurers and mandatory majority government shareholding in public insurers) poses significant challenges for insurers to maintain 150% solvency margins in a rapidly growing industry scenario.

3. **Technological advancement:** A key driver of growth in a long-term business like life insurance, technological advancement will be critical to functions like data management, underwriting, fund management, actuarial efficiency, and the end-to-end service delivery process. Technology will provide the cutting edge in terms of improved disclosure to the policy holder as well as the regulator in due course of time.

4. **Quality of manpower:** Insurance is an intensively people-oriented business and human resources will be the undoubted differentiator like in any other retail industry. The quality of manpower attracted and retained by insurers and how their abilities and ambitions are harnessed would be the litmus test for the industry

5. **Investment strategy and fund management:** Expertise in fund management is the value proposition that any insurance company offers and the quality of asset-liability management (ALM) in a falling or stable interest rate regime will thus be a key challenge. The regulator is progressively in favour of insurance companies setting up their own investment research and dealing cells and against knowledge sharing with group asset management companies. Bonus performance on traditional plans and the net asset value (NAV) performance on ULIPs will determine the demand patterns and investment strategy will remain at the core of successful insurance business.

6. **Meeting Cost Challenges:** Increasing the distribution reach to less populated areas will increase the costs of insurers. Such costs will have to be estimated and priced into the products. Issues relating to cross-subsidization may arise. Alternatively, insurers could introduce new products for these specific

market segments and price them to recover the incremental costs of their distribution. Controlling the distribution of specific products through agents has always been difficult. Another method of controlling costs by increasing productivity is to get agents to focus on particular generic products. Historically, this has been difficult to achieve and may not be in the best interests of the customer.

7. **Recruitment and selection of agents:** As stated earlier, attracting and retaining of agents is one of the major challenges. To overcome this challenge, the companies need to involve local management to recruit agents among the local population. For such wide recruitment efforts, local managers could be provided support in managing applications and conducting the selection process. Further, to ensure the success of this decentralization process it should become a part of the performance appraisal of the local management. Traditionally, the success rate of print advertisements attracting good applicants is very low. Unusual initiatives like presentations in social functions in clubs and meetings are expected to be powerful. Live examples of a few highly successful agents could be given during the presentations. The selection of agents should include behavioural traits and analytical abilities.

8.**Commission:** The agents work primarily on the commission which is paid to them on the basis of annualized premium per policy. The percentage of commission varies from product to product. There is no fixed remuneration to them. The IRDA guidelines prohibit paying any compensation to agents. It makes the early career phase of the agents difficult as they generally do not get too many policies in that phase. There is a need to find ways of overcoming the early phase difficulties and revising the existing norms. More help could be extended by sales managers to agents in the early phase to make them learn ways to get business. However, socially networked agents find it relatively easy to get more policies from their networks. In reality, an average agent is able to sell one to two policies per month.

There were 21, 09,718 agents as of end January 2015 as against 21,89,000 at the beginning of April last. While 5,03,000 new agents joined the sector since the beginning of this fiscal, as many as 5,83,000 agents have left the industry as of end January, resulting in a net attrition of 80,000 agents during the 10-month period, as per data. As per the existing system, up to 25 per cent of the first year premium is given to the agents as commission in traditional policies. However, this is a low 15 per cent in case of money-back policies and other ULIPS products. The new Insurance Act empowers IRDAI to finalise the agency commission structure. Also, it can enact regulations in such a way that commissions become attractive for the agents.

Other Challenges:

- Premium rates will remain under pressure due to intense competition on the more profitable lines.
- Public and private sector insurer's greater reliance on their investment portfolios to generate sufficient income and gains for net profits would subject them to the volatility of the financial markets.
- As far as the prospective are concerned, the greatest challenge is that of setting up infrastructure

and to reach out to as many areas as possible.

- The biggest challenge for public sector giant, the Life Insurance Corporation is one of the sustaining the huge growths it has shown in the recent times.
- Despite the liberalization in the insurance sector, public sector insurance companies are expected to maintain their dominant positions, at least in the foreseeable future.
- Falling premium income -- without a corresponding reduction in claims -- is likely to drive down profits
- Reinsurance is likely to cost more as treaty reinsurers reduce ceding commissions to compensate for the lower rates following deregulation
- Private insurers need to raise more capital, otherwise growth could be constrained since reliance on reinsurance for capital relief is not always viable or available
- Traditional distribution channels, especially tied agents, need to be improved to match the new product offerings
- There is general lack of transparency as financial and operational data for insurers are not readily available as none of India's insurers are directly listed on stock exchanges
- Like all developing economies on a fast track, the shortage of trained insurance professionals and technicians at all levels cannot be remedied in the short term
- Natural catastrophes will always be present; the Indian sub-continent is vulnerable to cyclones, floods, hurricanes and earthquakes, and until there is a national capacity (similar to the terrorism pool) to manage losses, dependence on overseas reinsurers will continue.

Opportunities

1. Social: The balance of power is shifting towards customers. New and ongoing social trends will shake up traditional business patterns in the insurance industry, resulting in an increase in consumer power:

- ***Customer expectations***: Customers (consumers and businesses) are increasingly demanding simplicity, transparency and speed in their transactions with businesses, including insurance agents/advisers and carriers. The relentless march of online and mobile technology is continuing to fuel this change in customer expectations. The online world is also becoming increasingly mobile as smartphone and tablet use increases and fuels the demand for localised information, available anytime, anywhere.

- ***Social networks***: The rapid adoption and fast evolution of social networks will continue to empower both consumers and businesses to communicate more transparently and to harness the buying power of virtual communities. The growth of social networking – one of the fastest ever global adoptions – will help shift the balance of power towards customers. In just six years since its launch, for example, Facebook has attracted over 800 million users. As consumers become even more comfortable with social networks several scenarios are likely to develop.

2. Technological: Advances in software and hardware that transform 'big data' into actionable insights. Historically, the insurance sector has been dominated by intermediaries who have played the role of understanding consumer and business needs, and then matching and tailoring insurance products and solutions to their needs. Internet, mobility and social networking have changed the game over the past decade and have created a new generation of customers who demand simplicity, speed and convenience in their interactions. These trends will accelerate, leading to a situation where customers will be more willing to buy 'direct' using their online and offline 'trust' network of friends and family to guide their choice. This will result in a fundamental redefinition of the role of advice and the disappearance of distributors as a sales channel.

3. Environmental: The rise of more sophisticated risk models and risk transfer to address the increasing severity and frequency of catastrophic events. Historically, the insurance sector has been good at developing catastrophic models that capture known high severity/low frequency events (e.g. earthquakes, tsunamis, etc.). However, most of these models perform poorly when it comes to unknown 'Black Swan' events. Over the next decade the insurance sector could be overwhelmed with uncorrelated catastrophic events reducing capacity and raising prices. Alternatively, new sensing and monitoring technology, together with risk transfer mechanisms, could cushion insurers and reinsurers against abnormal losses.

4. Economic: The rise of economic and political power in e merging markets. The increasing attractiveness of the emerging markets, combined with uncertain growth in the developed world and stricter regulatory guidelines will make carriers re-evaluate their strategic goals towards developing countries.

Other Opportunities:

- Aggressive marketing strategies by private sector insurers will maintain consumer awareness of risk and expand the markets for products.
- Competition in the insurance sector will allow market forces to set premiums that are appropriate for exposures and push insurers to differentiate their products and services.
- There is a probability of a spurt in employment opportunities.
- The falling interest rates, the scope for entering related areas like banking and pensions in a bit for synergy and the promise of e-commerce are some of the opportunities knocking at the door of the insurance sector.
- Given the enormous potential the Indian insurance market, it is expected that there will be enough business for the industry entrants.
- Privatization of Insurance eliminated the monopolistic business of Life Insurance Corporation of India. It helps to introduce new range of products which covered wide range of risks.
- It resulted in better customer services and help improve the variety and price of insurance products.
- The entry of new player has speed up the spread of both life and general insurance. It will increase the insurance penetration and measure of density.

- Entry of private players will ensure the mobilization of funds that can be utilized for the purpose of infrastructure development.
- The participation of commercial banks into insurance business helped to mobilization of funds from the rural areas because of the availability of vast branches of the banks.
- The intense competition brought about by deregulation has encouraged the industry to innovate in all areas; from underwriting, marketing, policy holder servicing to record-keeping
- Innovations in distribution and improvements in market penetration will follow as public and private insurers compete to market their products
- Allowing insurers to issue their own policy wordings and set their own rates will enable underwriters to tailor products to meet client needs
- The existence of stringent licensing requirements ensure that only adequately capitalized and professionally managed companies are eligible to carry out insurance and reinsurance
- The Insurance Regulatory Development Authority of India's (IRDA) emphasis on quarterly reporting/monitoring of insurer solvency will enhance capital adequacy and transparency.

The Insurance Laws (Amendment) Bill, 2015

A major economic reform in this year was the Insurance Laws (Amendment) Bill, 2015. The amended Law has several provisions for levying higher penalties ranging from up to Rs. 1 crore to Rs. 25 crore for various violations including mis-selling and misrepresentation by agents/insurance companies. It also disallows multi-level marketing of insurance products in order to curtail the practice of mis-selling. The amendments provide for an easier process for payment to the nominee of the policy holder, as the insurer would be discharged of its legal liabilities once the payment is made to the nominee. Insurance sector regulator, IRDA has been empowered to regulate key aspects of insurance company operations in areas like solvency, investments, expenses and commissions. In addition to the provisions for enhanced foreign equity to 49 per cent from 26 per cent, the amended law will enable capital rising through new and innovative instruments under the regulatory supervision of IRDA. IRDA is expected to frame guidelines to facilitate the entry of foreign players into the reinsurance business in the wake of the new Insurance Bill. It added that with a "view to serving the interest of the policy holders better", the period during which a policy can be repudiated on any ground will be confined to three years from the commencement of the policy and no policy would be called in question on any ground after three years.

Conclusion

From above discussion it is evident that life insurance expanded tremendously from 2000 onwards in terms of new business policies and premium business. The major drivers include sound economic fundamentals, a rising middle-income class, an improving regulatory frame work, and rising risk awareness. The fundamental regulatory changes in the insurance sector since 1999 were significant for future growth. Despite the restriction of 26 percent on foreign ownership, large foreign insurers

were entered in the Indian market. Private life insurers used the new business channels of marketing to a great extent when compared with the LIC. Indian insurance companies still have dominant market position. But this would probably change over the next decade.

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