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Impact of Liberalization of the Life Insurance Sector in India

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Abstract
Risk is an integral element of business and life in general. However, assumption of risk allows exploitation of the potentials of economic activities. In this context, the insurance sector plays a vital role in economic development of a country. Not only does insurance provide security against possible losses but the monetary resources mobilized by the sector acts as a source of long term finance to industry and infrastructure development. The insurance sector in India, comprising life and general insurance, has been historically government owned even after the introduction of liberalization measures for the rest of the economy. It was only in the year 2000 that the insurance sector, life and general, was opened up for the private sector. Foreign Direct Investment limit for the sector was liberalized from 26 percent to 49 percent only in 2014. Resultant to these developments, the number of life insurance companies increased from one to 24 over a period of time, while the total number of firms in the life and non-life segment together count to 57. The present study undertakes an examination of changes in the life insurance sector in India after liberalization of the sector. It inquires into how much privatization of the sector has happened after opening up of the sector to private investment.

Keywords: Insurance Sector, Life Insurance, FDI in Insurance Sector, Insurance Penetration, Insurance Density

Introduction

Insurance is a form of risk management technique which is used to transfer the risk of uncertainty or loss to a party willing to pool the risks of others. Insurance sector plays a dynamic role in the development of an economy. It substantially increases the opportunity of saving and safeguarding the future of an individual. The insurance sector in India is dominated by government owned insurance companies, both in life as well as non-life insurance segment. According to the Indian Insurance Industry Report of March 2019, of the 57 insurance companies 24 are into the segment of life insurance while 33 companies offer non-life insurance. The Life Insurance Corporation of India is largest and the only public sector life insurance company in India. However, with the further liberalization of the sector it is expected that new private insurers would take greater leaps in both Life and Non-Life Insurance.

The history of life insurance follows a similar path as the history of banking under the British rule. The origin of life insurance business can be traced to the establishment of the Oriental Life Insurance Company, set up by the British rulers in Calcutta in 1818. This was followed by the Bombay Assurance Company in 1823 and Madras Equitable Life Insurance in 1829 which aimed at providing Life Insurance to the Europeans living in India. The first Indian Life Insurance company, Bombay Life Insurance Society, was established in 1870 which provided Life Insurance to the lives of Indians. Later many companies were established which were then merged and formed into a giant in

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the life insurance sector in the post-independence period. The government nationalised the Life Insurance Corporation of India (LIC) which was established in 1956 after merging 245 life insurance companies in India. The General Insurance industry was nationalised with 4 subsidiaries in 1972.

In 1991 after India adopted the policy of liberalisation and as part of the WTO agreements the Government of India started considering opening up of the Insurance sector by allowing Foreign Direct Investment in India. FDI would help in boosting insurance penetration, providing a source of long term capital, creating new job opportunities and thereby economic growth. In 1994 the R.N. Malhotra Committee suggested opening up of Insurance sector to private participation. Finally, in 2000 it was opened for private sector allowing 26% FDI. The Insurance Regulatory and Development Authority of India (IRDAI) was set up in 2000 to regulate the Insurance sector. In 2014 with the Make in India initiative 49% FDI was allowed in Insurance sector. In the union budget of 2020 it is envisaged that government may propose to raise the FDI limit in Insurance sector to 74%.

Increase in the FDI limit has encouraged many foreign investors to increase their stake in Indian insurance joint ventures in the insurance sector. It is expected to attract more foreign investors in the sector instilling greater levels of competition. This is in turn is expected to lead to crafting of better and innovative insurance products which would meet the requirement of consumers. It would lead to better claim settlement, introduction of consumer friendly policies, greater availability of wider range of insurance products, improving customer services and growing market for insurance. The future prospect of the insurance sector also depends on the level and progress of financial access in the country which poses a great challenge given the poor levels of general and financial literacy as well as of income which causes high levels of exclusion.

Review of Literature

There are several studies on various aspects of Insurance sector found in literature. This section highlights some of the studies found in the field of insurance sector. Most studies analyze the trends and progress in the insurance sector in India. Narayana et al. (2012) have studied the trends in the life insurance sector in the pre and post liberalisation period, spanning from1998 to 2011. Jain (2013) has examined the impact of the 2008 economic crises on insurance sector in terms of the performance of life insurance companies and the opportunities and challenges faced by them.

Ahmed et al. (2013) have studied the performance of Life Insurance Corporation of India (LIC) and other private life insurance company in terms of insurance penetration and density. They find decreasing share of the public sector life insurance company over the years. Arif (2015) has examined the trend and pattern in the life insurance sector in India based on the secondary data in the post liberalisation period from 2003-04 to 2012-13. He has used statistical tools such as simple ratios and growth rates along with regression analysis to analyse the data. The performance of life insurance is measured with two parameter i.e. insurance penetration and insurance density.

Shikhare (2015) has investigated the benefits of increase in FDI limit in insurance sector also and tried to find out the issues in FDI in insurance sector. He concluded that FDI helps in increasing insurance penetration, job creation, and introduction of consumer friendly products as well as better claim settlement ratio.

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Hassan (2015) has examined the opportunities and expansion due to FDI in Insurance sector in India and the major challenges faced by foreign insurance companies. Chandra Kantha et al. (2016) have studied the significance of FDI in insurance sector by analysing the opinion of both private and public insurance companies in India. He has used questionnaire method for data collection and selected a sample size of 60 executives across public and private sector.

Vikas (2016) has examined the impact of liberalisation in life insurance business in India and compared the performance of public and private sector life insurance business in India. His study is based on secondary data and the period of study was from 2000-01 to 2015-16. He has analysed the performance and growth with new policies issued, premium and market share. His study reveals that the market share of LIC has decreased consistently.

Kumar (2016) has examined the impact of liberalisation in penetration and density in the post reform period for private insurers and LIC. He has compared the strength of the insurance companies measured by their solvency ratio, that is, the ability to honour the claims of the clients.

Santimol et al. (2018) have emphasised on the performance, competition, concentration and profitability in select life insurance company in Kerala. The researcher has used concentration ratio (CR5) and Herfindahl- Hirschman index (HHI) to measure the level of concentration in the sector in Kerala and compared the financial performance of the companies using Return on Assets and Return on Equity to measure performance. For analysing market concentration HHI is used between LIC, SBI life, ICICI prudential, HDFC life and Bajaj Allianz. For profitability analysing financial ratio ROA and ROE is used. Data Envelopment Analysis has been carried out based on variables such as operating expense, commission paid and labour cost as inputs and premium earned, claim settled and income from investment as output. They find that the sector is lacking in efficiency and their performance has been inconsistent.

Scope of Study

From the brief review of literature it is found that most of the studies are focusing on the market structure of the insurance sector and analysing the performance of the life insurance companies. Studies on trends in the sector typically analyze the depth of the sector. The present study traces the privatization of the life insurance sector and undertakes a preliminary examination the pace of growth and efficiency of the private life insurance players vis-a-vis The Life Insurance Corporation of India (LIC).

Objectives

The objectives of the present study as are follows:

- To examine the impact of liberalisation by way of privatization and FDI in Life Insurance sector in India.
- To examine the growth and efficiency of private insurance companies vis-a-vis LIC
- To analyse the trend and progress in Life Insurance sector.

Research Methodology

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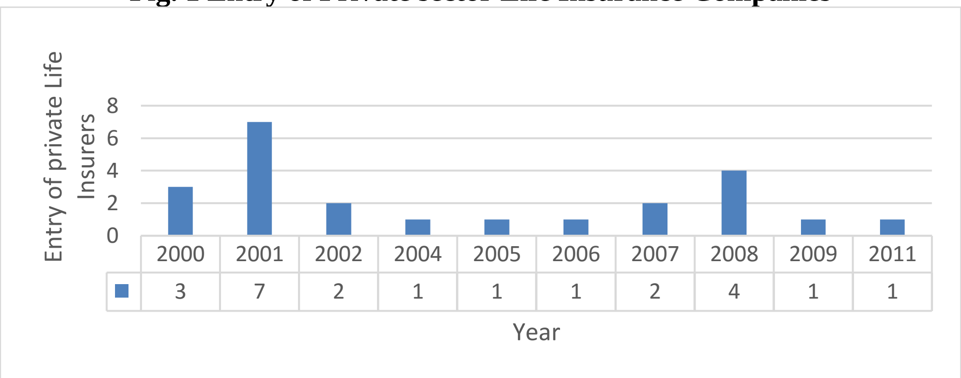
The present study is a descriptive and analytical research. It is based on secondary data sourced from reports of IRDA and LIC. The period of study is 2000 to 2018. The impact of liberalization of the sector is measured in terms entry of private companies, Insurance Penetration, Insurance Density and change in the structure of the market of life insurance business in India. Statistical tools like simple tabulation, growth rates, ratios etc., have been used.

Entry of Firms after Liberalisation

It is going to be two decades now when the Government of India liberalised the insurance sector by allowing 26% FDI. There are currently 24 life insurance companies in India. Some domestic private companies are operating as independent companies while some are joint ventures with nationalized banks and with foreign financial services companies. Since liberalisation many Indian and foreign companies are approaching for setting up a Joint venture business in Life insurance sector. Currently 23 private sector life insurance companies are operating in India. Of these, 20 are in collaboration with foreign partners. In other words, liberalization of FDI norms has resulted into 20 foreign companies entering into the sector. Fig.1 depicts the entry of private sector life insurance companies after liberalization of the sector in 2000. It can be observed that opening up of the sector evoked interest in the sector with ten companies entering within the first two years. Thereafter, there is a subdued entry of new firms. Increase in the FDI limit from 26% to 49% in the year 2014, has not resulted into new firms entering the sector.

Fig. 1 Entry of Private sector Life Insurance Companies



Source: IRDA, Handbook on Indian insurance statistics F.Y. 2017-18

Expansion of the Life Insurance Companies

Expansion of life insurance can be measured with the growth of number of offices in both private sector and LIC. Although the number of private sector insurance company offices in the year 2001 was only 13, it expanded to as high as 8785 in 2009. This shows that there was a rapid expansion by the private players in their operations. The slowdown of the economy post 2008 global financial crises appears to have led to consolidation in the number of offices with their number consistently reducing to 6193 in 2014. In the last four years of the study period the number of offices of the private insurance companies has fluctuated in a narrow range up to 6204 in 2018 as depicted in Fig.2.

Fig. 2: No. of Offices of Life Insurance Companies

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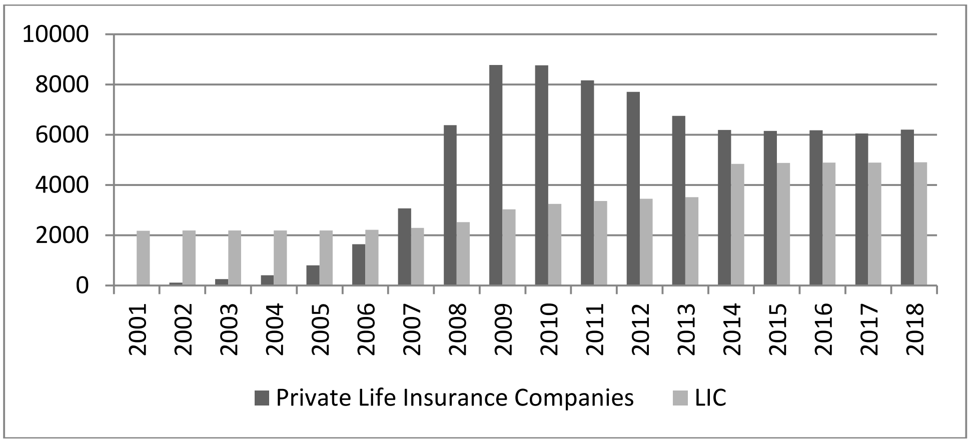
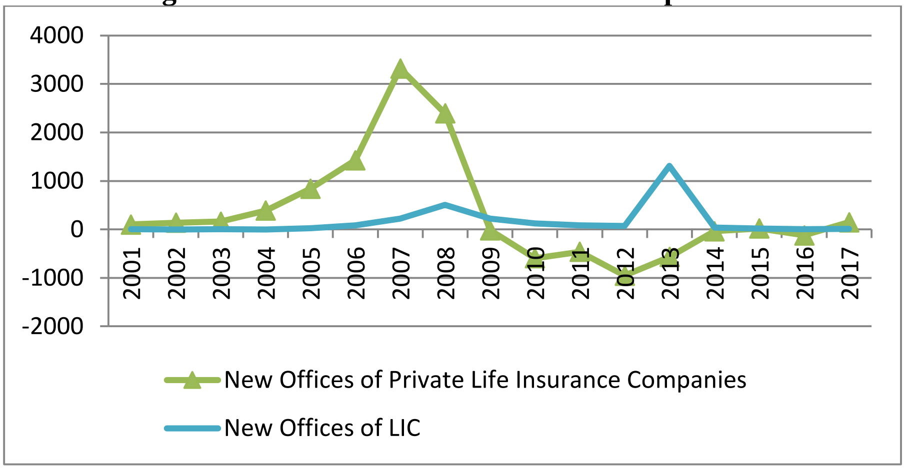


Source: IRDA Reports

The number of offices of LIC after liberalisation was 2186 which has a gradual increasing trend to 2301 in 2007. After that the pace of increase in number of offices has increased for LIC from 2500 plus to 4908 in 2018. While the number of offices of LIC has consistently increased, private sector companies have adopted the approach of consolidation and rationalization by reducing the number of offices.

The growth in the number of offices each year in the private and public sector life insurance sector is depicted in Fig.3. It can be seen that between 2009 and 2014 there is much rationalization in the number of offices of private life insurance companies.

Fig. 3: New Offices of Life Insurance Companies



Growth of Insurance Sector in the Post Liberalization Phase

Insurance Penetration and Insurance Density is a measure which is the major indicator of development of Insurance sector in a country. Insurance Penetration is measured by the premium collection by life insurance companies as a percentage of GDP. Insurance Density is measured as the ratio of insurance premium to the total population of a country. Fig. 4 shows the trends in the two measures.

Fig. 4: Life Insurance Penetration and Density

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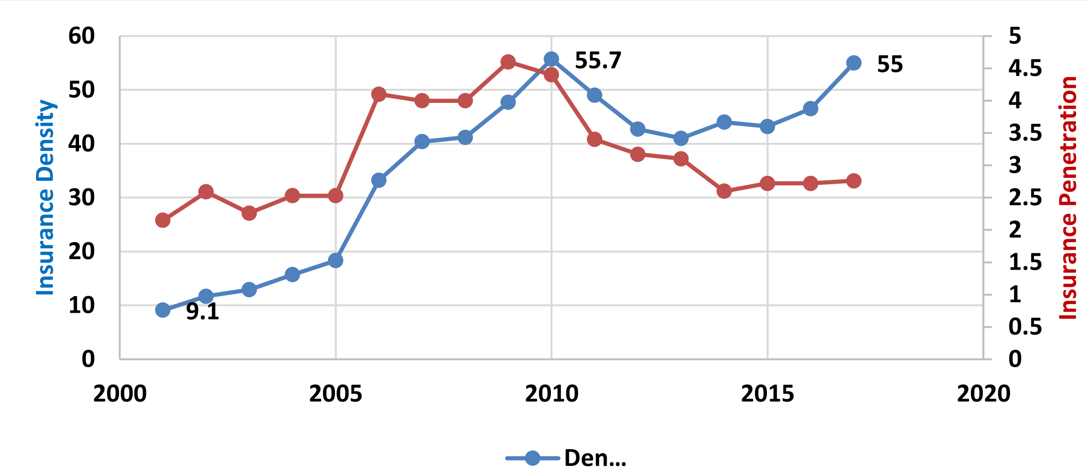
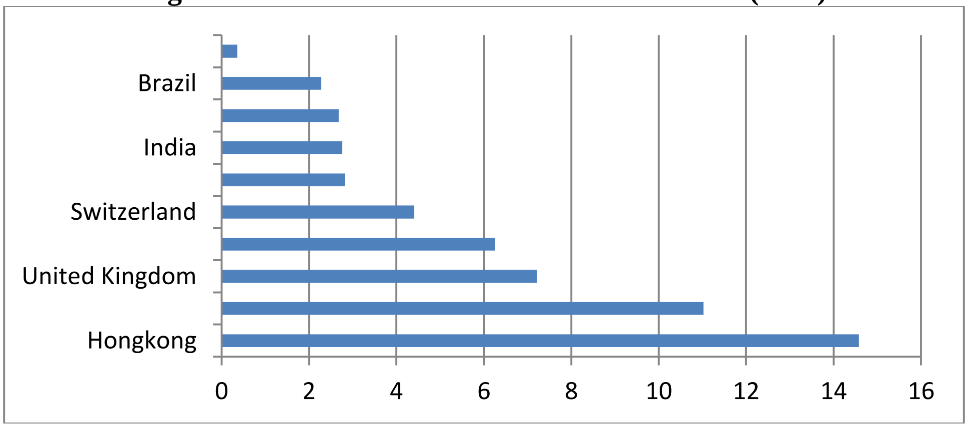


Blue line: Insurance Density Red line: Insurance Penetration

Source: IRDA Reports and Handbook on Indian Insurance

Insurance Penetration has consistently increased from 2.15% in 2001 to 4.60% in 2009 in life insurance sector after which there has been a constant decline. Liberalization of the sector has led to faster pace of coverage of population under life insurance, that is, Insurance Density, from 9.10 USD Billion to 55.70 USD Billion between 2001 and 2010. To put the insurance penetration in India in perspective, Fig 5 depicts the relative position of India vis-a-vis BRICS countries and select advanced countries. It may be noted that India compares well with Brazil and China and with US but is much below South Africa which claims insurance penetration of eleven percent. Similar picture emerges in the case of insurance density.

Fig. 5 Insurance Penetration in Select Countries (2017)



Source: World Bank Database

Life Insurance Premium Collection

Total premium is the combined contribution of New Business Premium and Renewal Premium. New Business Premium is the sum total of First Year Premium and Single Premium. Table 1 shows the premium collection against life insurance schemes for private players and the LIC. The private insurers' total premium in 2000 was Rs. 6.45 crore which increased to Rs.88165.24 crore in 2010. After this the private insurers' premium started decreasing. In the last four years of the study period, there has been an increasing trend with total premium Rs.140586.23 crore for the year 2017. For the

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entire period of study, their premium collection has grown by the compound annual growth rate of almost 80 percent. It is noteworthy that in the first decade of operations, private insurers' premium collection has increased at a high CAGR of 184 percent while in the second decade under study the CAGR slowed down to 7.41 percent.

At the time of liberalisation of the sector in the year 2000-01, LIC had a total premium collection of Rs.34892.02 crore which increased to Rs.318223.21 crore in 2018. The CAGR of LIC is much lower at 14 percent; however, it is on the base of a much higher value. For LIC too, the CAGR is higher at 20.44 percent in the first decade of the study period and has thereafter has reduced to almost seven percent.

Table 1: Total Life Insurance Premium Collection (in INR Crore)

Year	Private Companies	LIC
2000-01	6.45	34892.02
2001-02	272.55	49821.91
2002-03	1119.06	54628.49
2003-04	3120.33	63533.43
2004-05	7727.51	75127.29
2005-06	15083.54	90792.22
2006-07	28253.00	127822.84
2007-08	51561.42	149789.99
2008-09	64497.43	157288.04
2009-10	79369.94	186077.31
2010-11	88165.24	203473.40
2011-12	84182.83	202889.28
2012-13	78398.91	208803.58
2013-14	77359.36	236942.30
2014-15	88434.36	239667.65
2015-16	100499.03	266444.21
2016-17	117989.25	300487.36
2017-18	140586.23	318223.21

Source: IRDA Reports

The extent of privatization of the life insurance sector can be judged from the fact that in the year 2000-01, the premium collection of LIC was 5409 times higher than that of the private players which is obvious because the latter had just entered into the business, however, in the year 2017-18 this ratio has reduced to 2.26. This underlines the acceleration in the growth of private players in the sector leading to lowering of gap the between the two sectors. The composition of total premium collection in terms of LIC and private insurers is depicted in Fig.6.

Fig. 6 Distribution of Insurance Premium Collection into Private and Public Sector

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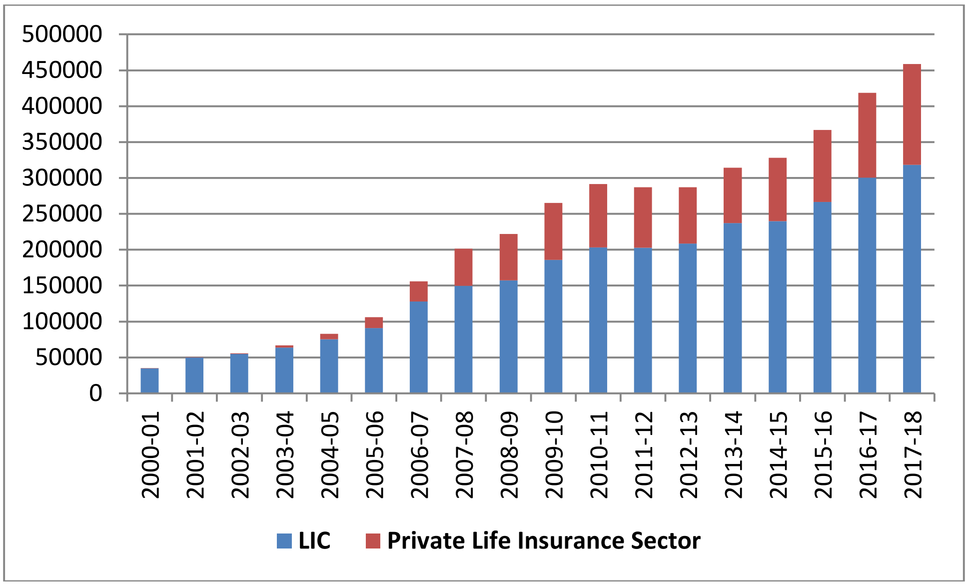
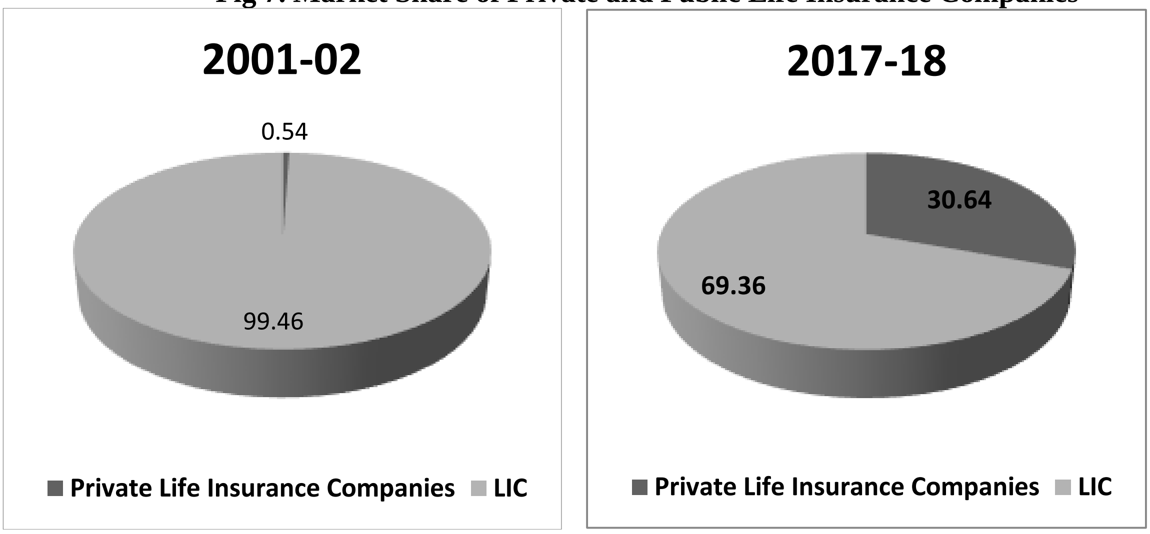


Market Share of Private and Public Sector Life Insurance Companies

In terms of market share of private sector companies vis-a-vis LIC, the only public sector company, the dominance of LIC is clearly established. In the year 2001 when liberalisation was adopted for the sector, the market share of private sector in 2001 was only 0.54% and that of LIC was 99.46%. (Fig.7). However, in the year 2017-18 private insurers' market share is 30.64% and that of LIC is 69.39% which indicates a substantial market gain by the former. Although the market share of LIC is deteriorating and private insurer is increasing but, still LIC is dominating the whole Life Insurance sector.

Fig 7. Market Share of Private and Public Life Insurance Companies



Source: IRDA various Handbook

Efficiency of the Life Insurance Sector

This section undertakes a preliminary examination of the efficiency of the life insurance companies in India. Efficiency has been measured in a crude fashion in terms of premium collection per office. It has been computed by dividing the premium collection by the number of offices for private and public players separately. Fig. 8 depicts the trends in efficiency for the sector. It is evident that there

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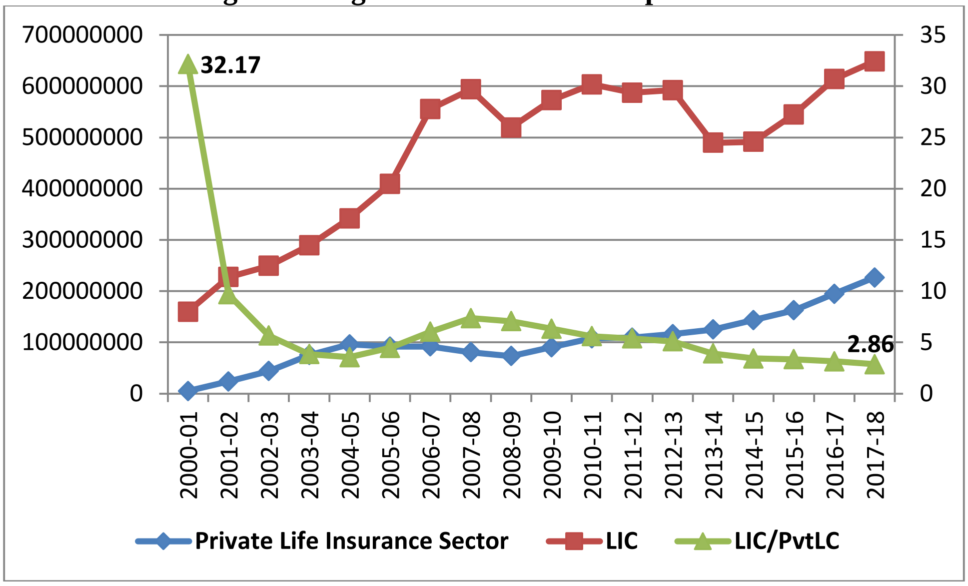
are efficiency gains in the case of both LIC and the private companies as can be seen from the increasing trend in the average premium collection per office over the years. The efficiency of LIC is much higher than that of the private companies given its history of large number of agents and its geographical spread across the country. The right hand scale of Fig.8 shows the ratio of the average premium collection of LIC per office to that of the private companies. A striking observation is that at the point of entry of private players in the life insurance sector in India, the average premium collection of LIC was 32 times higher than that of its private counterpart. However, in the second year there can be seen a sharp decline in this ratio to 9.68 which has further fallen to 2.86 in the year 2018. The simple measure of efficiency gains in terms of average premium per office underlines the acceleration in the pace of operations of the private life insurers. With further liberalization of the FDI norms, it is expected that this trend would become more and more pronounced with entry of more private players, both domestic and foreign.

Fig. 8 Average Premium Collection per Office



Source: Computations based on data from IRDA Reports

Conclusion

The analysis of the life insurance sector in the post liberalization era shows rapid increase in the privatization of the sector. LIC continues to dominate the sector but equally significant is the pace of growth of the private companies in gaining greater market share over the years. Much of this growth may be attributed to the aggressive product and pricing policies adopted by them. Given the huge scope of growth in the sector, it is bound to attract more private players with foreign counter parts in to the sector, infusing greater competition. The future prospects of the sector can be gauged by the fact that insurance penetration and density is amongst the lowest in India. This suggests huge scope for the sector to grow in the future supported by policy measures.

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