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INDIA'S INSURANCE SECTOR: CHALLENGES AND OPPORTUNITIES

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Key Highlights

- India's insurance sector has been growing dynamically in the last couple of years. Having grown and evolved to a great degree, it has emerged from a public monopoly and restricted market to a competitive and open one. The paper analyses the Indian insurance sector, tracing its evolution and growth, and identifies the key challenges facing the sector.
- Despite the suite of reforms that have been implemented to stoke the sector's growth, it still has a long way to go, as its share in the global insurance market remains abysmally low.
- As underlined in the paper, low penetration and density rates, less investment in insurance products, dominant position of public sector insurers, and their deteriorating financial health are some of the challenges facing the sector.
- Since India's economic growth depends on how shock-absorbent India's economy is, addressing these challenges to develop a sound insurance sector assumes importance.

EXECUTIVE SUMMARY

In this paper, we trace the journey of the Indian insurance sector and identify the challenges facing the insurance sector.

INSURANCE INDUSTRY IN INDIA

The insurance industry in India has been growing dynamically, with the total insurance premiums increasing rapidly compared with its global counterparts. In the past 17 years or so, the insurance sector of India has risen at a compound annual growth rate (CAGR) of 16.5 per cent. The insurance penetration and density stood at 3.69 per cent and USD 73 respectively for FY2017-18, which is low in comparison with global levels. These low penetration and density rates reveal the uninsured nature of large sections of population in India and the presence of an insurance gap.

Although India's insurance penetration and density are low compared to advanced countries in both life and non-life insurance sectors, in recent years they are showing a slow but steady growing trend. The industry has experienced a sea change in the last couple of years, wherein it has been shaped for a large part by nationalisation of life and non-life sectors, constitution of the IRDA, opening up of the sector for both private and foreign players and increase in the foreign investment cap to 49 per cent. The recent notification of 100 per cent foreign direct investment for insurance intermediaries has further liberalised the sector. The sector has transitioned from being an exclusive state monopoly to a competitive market, but public sector insurers continue to have the upper hand in the market. Further, life insurance dominates the sector with a huge share of 74.73 per cent, with non-life insurance accounting for 25.27 per cent.

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THE INDIAN INSURANCE SECTOR AT A GLANCE

The measures of insurance penetration (percentage of insurance premium to GDP) and density (ratio of insurance premium to population or per capita premium) reflect the level of development of the insurance sector in a country. Table 1 documents the insurance penetration and density in India from 2001 to 2017.

India's insurance penetration and density remain low in comparison with its global counterparts. The total insurance penetration and density rates stood at 3.69 per cent and USD 73 respectively in 2017. India emerges a laggard in terms of penetration and density even in comparison with the BRICS countries. Public sector insurers hold a greater share of the insurance market even though they are fewer in number. Nevertheless, private sector insurers are slowly increasing their market share in both life and non-life segments.

SECTORAL SNAPSHOTS OF INDIA'S INSURANCE MARKET

Life insurance dominates the sector, with a huge share of 74.7 per cent, with non-life insurance accounting for 25.3 per cent market share, as per the IRDAI's Annual Report 2017-18. According to data published by Swiss Re, India's share in the global life insurance market was 2.7 per cent during 2017.

In the non-life insurance sector, motor, health, and crop insurance segments are driving growth. India's non-life insurance penetration is below 1 per cent, which, in comparison with global levels of developed and emerging economies, is extremely low. In addition, insurance products catering to speciality risks such as catastrophes and cyber security are at a nascent stage of development in India.

These low penetration and density rates reveal the uninsured nature of large sections of population in India and also the presence of an insurance gap. Lloyd's (2018) put this gap at a staggering USD 27 billion in absolute terms. The reasons cited for such minimal levels of penetration rates include tight constraints on the household budget, adverse selection, moral hazard, and affordability issues (Household Finance Committee, 2017).

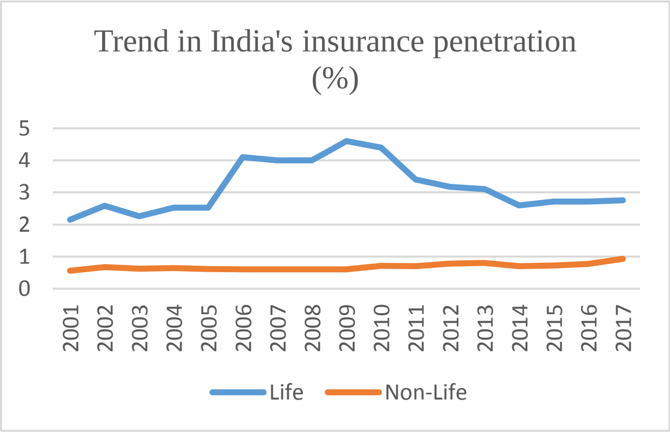
REINSURANCE SECTOR IN INDIA

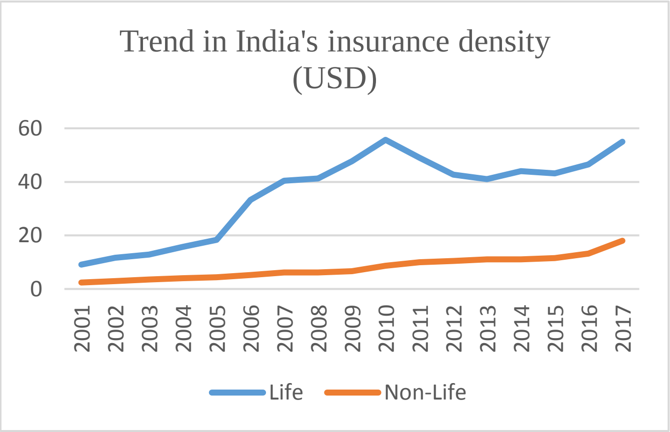
The Indian experience with reinsurance can be assessed with respect to the nationalisation of the general insurance sector, as well as the liberalisation of the insurance sector. With the merger of the former general insurance companies, GIC assumed the role of a parent body supervising general insurers and arranged reinsurance for insurers with a common integrated reinsurance programme. These changes have been instrumental in shaping the reinsurance market in India to its current form. From the earlier confinement of the reinsurance market to only the public sector reinsurer GIC Re, the market has in due course been opened up to private reinsurers, as well as branches of foreign reinsurers. The life reinsurance market is relatively small vis-à-vis non-life reinsurance in India. Catastrophic insurance in India is at a very nascent stage of development, as very few property insurance products in India extensively cover natural disaster risks.

EMPIRICAL ANALYSIS

The crucial place occupied by insurance in the macroeconomic development of an economy is acknowledged. The insurance sector can influence macroeconomic development via a range of channels

Figure 1: Trend in India's insurance penetration (%) and Trend in India's insurance density (USD)





Source: IRDAI Annual Report 2018

Table 1: Insurance penetration and density in India

Year	Life		Non-life		Industry	
	Density (USD)	Penetration (%)	Density (USD)	Penetration (%)	Density (USD)	Penetration (%)
2001	9.1	2.15	2.4	0.56	11.5	2.71
2002	11.7	2.59	3.0	0.67	14.7	3.26
2003	12.9	2.26	3.5	0.62	16.4	2.88
2004	15.7	2.53	4.0	0.64	19.7	3.17
2005	18.3	2.53	4.4	0.61	22.7	3.14
2006	33.2	4.10	5.2	0.60	38.4	4.80
2007	40.4	4.00	6.2	0.60	46.6	4.7
2008	41.2	4.00	6.2	0.60	47.4	4.60
2009	47.7	4.60	6.7	0.60	54.3	5.20
2010	55.7	4.40	8.7	0.71	64.4	5.10
2011	49.0	3.40	10.0	0.70	59.0	4.10
2012	42.7	3.17	10.5	0.78	53.2	3.96
2013	41.0	3.10	11.0	0.80	52.0	3.90
2014	44.0	2.60	11.0	0.70	55.0	3.30
2015	43.2	2.72	11.5	0.72	54.7	3.44
2016	46.5	2.72	13.2	0.77	59.7	3.49
2017	55.0	2.76	18.0	0.93	73.0	3.69

Source: IRDAI Annual Report, 2017-18.

due to the presence of a myriad of linkages between them. Many studies have offered empirical support to the cogent link between insurance and economic growth. Only a handful of studies (Verma and Bala, 2013; Ghosh, 2013; Kaushal and Ghosh, 2016) have attempted to examine the links in the Indian context. A simple regression exercise shows the relationship between insurance and economic growth in the Indian case from 1990-91 to 2017-18. Three equations have been estimated for life, non-life, and total insurance penetration. Results of the regression show a positive and significant relationship between insurance penetration rates (life, non-life, and total) and economic growth in India. Further, the influence of liberalisation (increasing of the FDI cap to 49 per cent) has been tested by introducing a year dummy. Results indicate that liberalisation positively influenced the life and total insurance penetration rates. The effect on non-life insurance penetration rates is negative and insignificant. The effect of demonetisation has also been tested by adopting a similar dummy variable approach, as demonetisation led to a sudden and transient surge in premium growth. Results reveal a positive and significant impact of demonetisation on insurance (life and total) penetration rates, whereas the impact on non-life insurance is positive but insignificant.

KEY CHALLENGES AND OUTLOOK

The Indian insurance sector faces various challenges as identified and detailed in the paper. Low insurance penetration and density rates prevail in India. Rural participation of insurers remains deficient, and life insurers, especially private ones, gravitate towards the urban population, to the detriment of the rural population. The dominant position of state-owned insurers is proving to be a cause for concern for private sector insurers as well as foreign insurers. Adding to the list of problems, insurers in India lack sufficient capital, and their financial health, particularly that of the public sector insurers, is in a precarious state. Further, there are concerns in the non-life insurance sector regarding product pricing and overcrowding in some segments, along with issues in the crop insurance segment. Besides these key challenges, other challenges such as the prevalence of traditional distribution channels also hinder the sector's growth.

India's insurance sector has potential to grow further due to the underpenetrated nature of the market and low density. Demographic factors, coupled with increasing awareness and financial literacy, are likely to catalyse the growth of the sector.

CONCLUSION

The paper has assessed the evolution and growth of India's insurance sector and identified the challenges that have stymied the development of the sector. Even after implementing a gamut of reform measures, the Indian insurance sector still has a long way to go in order to be comparable to other advanced economies' insurance sectors. India's share in the global insurance market is abysmally low. To increase its share globally, the underlying challenges will have to be addressed.

India's economic growth depends on how shock-absorbent India's economy is. Both financial and climatic shocks (which are on the rise, given climate change) are important for India and having an efficient and stable insurance market in place determines India's growth performance in both the short and long terms.

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